

85 - 1988

No.

Supreme Court, U.S.  
FILED

MAY 30 1986

JOSEPH F. SPANIOL, JR.  
CLERK

---

**In The  
Supreme Court  
Of The United States**

**October Term, 1985**

---

**TYLER PIPE INDUSTRIES, INC.,**

*Appellant*

vs.

**STATE OF WASHINGTON DEPARTMENT OF REVENUE,**

*Appellee*

---

**On Appeal from the  
Supreme Court of Washington**

---

**JURISDICTIONAL STATEMENT**

---

NEIL J. O'BRIEN  
GARDERE & WYNNE  
1500 Diamond Shamrock  
Tower  
Dallas, Texas 75201  
(214) 979-4500

*Counsel for Appellant*

83P2

**In the  
Supreme Court of  
the United States**

October Term, 1985

---

**No.**

TYLER PIPE INDUSTRIES, INC.,

*Appellant*

vs.

STATE OF WASHINGTON DEPARTMENT OF REVENUE,

*Appellee*

---

**On Appeal from the  
Supreme Court of Washington**

---

**JURISDICTIONAL STATEMENT**

---

**QUESTIONS PRESENTED**

Sections 82.04.220 *et seq.*, of the Revised Code of the State of Washington, impose a business and occupation tax upon persons engaged in, *inter alia*, wholesaling and manufacturing, measured by gross receipts received from the activity. Section 82.04.440 of the Revised Code provides an exemption from the manufacturing tax for persons engaged in both manufacturing and wholesaling within the State of Washington.

The questions presented are:

1. Whether the Washington Supreme Court disregarded the standards enunciated by this Court in *Armco, Inc. v. Hardesty*, U.S. , 104 S.Ct. 2620, rehearing denied, U.S. , 105 S.Ct. 285 (1984) and *Maryland v. Louisiana*, 451 U.S. 725 (1981) in deciding the case below?

2. Whether the Washington statutory scheme violates the Commerce Clause of the United States Constitution because the tax imposed discriminates against interstate commerce?

3. Whether the Washington statutory scheme violates the Commerce Clause of the United States Constitution because the tax imposed is not fairly apportioned, or is not fairly related to the services provided by the State of Washington?

4. Whether, as applied to Appellant, the tax imposed by these statutory provisions violates the Due Process Clause or the Commerce Clause of the United States Constitution because Appellant's connections with the State of Washington are insufficient to satisfy constitutional standards with respect to nexus?

### LIST OF PARTIES

The names of all parties to the proceedings below are reflected in the caption of the case. Pursuant to Supreme Court Rule 28.1, the Appellant, Tyler Pipe Industries, Inc., a Delaware corporation with its principal office in Tyler, Texas, states that it is a wholly-owned subsidiary of Tyler Corporation. There are no other parent corporations, subsidiaries or affiliates of Appellant or Tyler Corporation other than wholly-owned subsidiaries of each.

### TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED .....	i
LIST OF PARTIES.....	ii
OPINIONS BELOW .....	1
JURISDICTION .....	1
CONSTITUTIONAL PROVISIONS AND STATUTES .....	1
STATEMENT OF THE CASE .....	2
THE QUESTIONS ARE SUBSTANTIAL .....	7
I. The Washington B&O tax discriminates against interstate commerce .....	7
II. The Washington B&O tax is not fairly appor- tioned and is not fairly related to services provid- ed by the state .....	12
III. As applied to Appellant, the Washington B&O tax is unconstitutional because a sufficient nexus does not exist between Appellant's activities and the state .....	13
CONCLUSION .....	16
APPENDICES	
A. Opinion of Washington Supreme Court .....	A-1
B. Opinion and Findings of Fact, Conclusions of Law and Judgment of Superior Court of Thur- ston County .....	B-1
C. Determination and Final Determination of the State of Washington Department of Revenue ..	C-1
D. Opinion of Washington Supreme Court in <i>Na-         tional Can Corp. et al. v. State of Washington</i> .	D-1
E. Judgment sought to be reviewed .....	E-1
F. Notice of appeal .....	F-1
G. Constitutional provisions and statutes .....	G-1

## TABLE OF AUTHORITIES

	<u>Page</u>
CASES:	
<i>Armco, Inc. v. Hardesty</i> , U.S. , 104 S.Ct. 2620, rehearing denied, U.S. , 105 S. Ct. 285 (1984) .....	7, 9-13, 16
<i>Boston Stock Exchange v. State Tax Commission</i> , 429 U.S. 318 (1977).....	8
<i>Chicago Bridge and Iron Co. v. Department of Revenue</i> , 98 Wn.2d 814, 659 P.2d 463 (1983), appeal dismissed, 464 U.S. 1013 (1983) .....	3
<i>Complete Auto Transit, Inc. v. Brady</i> , 430 U.S. 274, rehearing denied, 430 U.S. 976 (1977) .....	7, 12
<i>General Motors Corporation v. Washington</i> , 377 U.S. 436 (1964) .....	10, 12
<i>Gwin, White &amp; Prince, Inc. v. Henneford</i> , 305 U.S. 434 (1939) .....	8
<i>Maryland v. Louisiana</i> , 451 U.S. 725 (1981) ....	7-10
<i>McLeod v. J. E. Dilworth Company</i> , 322 U.S. 327 (1944) .....	14
<i>Mobil Oil Corp. v. Commissioner of Taxes of Vermont</i> , 445 U.S. 425 (1980) .....	8
<i>National Bellas Hess, Inc. v. Department of Revenue</i> , 386 U.S. 753 (1967).....	14
<i>National Can Corp. v. Department of Revenue</i> , 105 Wn.2d 327, 715 P.2d 128 (1986) .....	1, 3, 9
<i>Northwestern States Portland Cement Co. v. Minnesota</i> , 358 U.S. 450 (1959) .....	8

	<u>Page</u>
<i>Norton Company v. Department of Revenue of the State of Illinois</i> , 340 U.S. 534 (1951) .....	14-16
<i>Scripto, Inc. v. Carson</i> , 362 U.S. 207 (1960) .....	13-14
<i>Standard Pressed Steel Company v. Washington Department of Revenue</i> , 419 U.S. 560 (1975) ..	13-14
CONSTITUTIONAL PROVISIONS:	
U.S. Constitution, Amendment XIV, Section 1 (Due Process Clause) .....	1-3, 7
U.S. Constitution, Article I, Section 8, clause 3 (Commerce Clause) .....	1-3, 7-10
STATUTES:	
Federal Interstate Income Tax Act, 15 U.S.C. Sections 381 <i>et seq.</i> .....	1-3, 14-15
Revised Code of Washington:	
Section 82.04.220 .....	2, 6
Section 82.04.230 .....	2, 8
Section 82.04.240 .....	2, 6, 8-9
Section 82.04.250 .....	2, 8
Section 82.04.270 .....	2, 6, 8-9
Section 82.04.290 .....	2, 8
Section 82.04.440 .....	2, 6, 8-9
Section 82.04.500 .....	2, 6
MISCELLANEOUS:	
W. Hellerstein, "Constitutional Limitations on State Tax Exportation," 1982 <i>American Bar Foundation Research Journal</i> 1 (1982) .....	8

Tyler Pipe Industries, Inc., the Appellant, appeals from the final judgment of the Supreme Court of Washington rendered in this case on March 6, 1986. This jurisdictional statement is submitted to show that the Court has jurisdiction of the appeal and that substantial questions are presented.

### **OPINIONS BELOW**

The opinion of the Supreme Court of the State of Washington (Appendix A, *infra*, p. A-1) is reported at 105 Wn.2d 318 and 715 P.2d 123. The opinion of the Superior Court for Thurston County, Washington (Appendix B, *infra*, p. B-1) is not officially reported. The determination and final determination of the State of Washington Department of Revenue (Appendix C, *infra*, p. C-1) are not officially reported. The opinion of the Supreme Court of the State of Washington in the companion case of *National Can Corporation v. The State of Washington* (Appendix D, *infra*, p. D-1) is reported at 105 Wn.2d 327 and 715 P.2d 128.

### **JURISDICTION**

Appellant brought this action in the Superior Court of Thurston County, Washington, seeking a refund of business and occupation taxes imposed by the State of Washington. The Supreme Court of Washington entered and filed its opinion and judgment on March 6, 1986. Appellant filed a notice of appeal in that court on April 15, 1986. Jurisdiction of this Court is invoked under 28 U.S.C. Section 1257(2). Alternatively, the jurisdiction of this Court is invoked under 28 U.S.C. Section 1257(3). *See*, 28 U.S.C. Section 2103.

### **CONSTITUTIONAL PROVISIONS AND STATUTES**

The relevant provisions of the United States Constitution, Article I, Section 8, clause 3; of the United States Constitution, Amendment XIV, Section 1; of 15 U.S.C. Section 381; and of the

Revised Code of Washington, Sections 82.04.220, 82.04.230, 82.04.240, 82.04.250, 82.04.270, 82.04.290, 82.04.440 and 82.04.500 are set forth at Appendix G, *infra*.

## STATEMENT OF THE CASE

### 1. Proceedings Below; Federal Question Raised

The Department of Revenue for the State of Washington assessed business and occupation taxes (hereinafter referred to as "B&O taxes") for the period January 1, 1976 through September 30, 1980 against Appellant, Tyler Pipe Industries, Inc. Appellant petitioned the Department of Revenue for correction of the assessment on the grounds that imposition of the tax against Appellant violated a federal statute and the U.S. Constitution. The Department denied the petition. Appellant then sought a temporary injunction in the Superior Court for Thurston County, Washington, against the Department's collection of the assessment. In its complaint, Appellant asserted that the assessment violated the Due Process and Commerce Clauses of the United States Constitution and the Federal Interstate Income Tax Act, 15 U.S.C. Sections 381 *et seq.* The Superior Court granted the injunction on June 8, 1981. The grant of the injunction was reversed by the Supreme Court of the State of Washington on January 4, 1982 on the grounds, *inter alia*, that Appellant was not likely to succeed on the merits of its constitutional claims.

Appellant paid the tax assessment on March 10, 1982 and sued for refund in the Superior Court for Thurston County, State of Washington, on the grounds that assessment and collection of the tax violated the Due Process and Commerce Clauses of the United States Constitution and the Federal Interstate Income Tax Act. The Superior Court filed a memorandum opinion dated June 15, 1984 in which it held that the tax did not violate the Due Process Clause because the tax is fairly apportioned and there was a sufficient nexus between Appellant and the State of Wash-

ington to justify imposition of the tax (Appendix B, *infra*, p. B-4). The latter conclusion was based on activity performed in the state by independent sales representatives. The court also concluded that the tax did not violate the Commerce Clause because the tax treats interstate and intrastate commerce equally and because the tax is fairly related to services provided by the state (Appendix B, *infra*, p. B-6). The court rested these conclusions on the decision of the Washington Supreme Court in *Chicago Bridge and Iron Co. v. Department of Revenue*, 98 Wn.2d 814, 659 P.2d 463 (1983), *appeal dismissed*, 464 U.S. 1013 (1983). Finally, the court found the Federal Interstate Income Tax Act inapplicable to the Washington B&O tax (Appendix B, *infra*, p. B-6). The Superior Court denied Appellant's motion for reconsideration on August 6, 1984, and entered Findings of Fact, Conclusions of Law, and Judgment on October 24, 1984 (Appendix B, *infra*, pp. B-7 to B-15).

Appellant timely filed its Notice of Appeal to the Washington Supreme Court on November 9, 1984, raising as error each of the issues raised and rejected in the Superior Court. The Washington Supreme Court filed its opinion on March 6, 1986, affirming the Superior Court in all respects (Appendix A, *infra*, p. A-1). The court dealt first with the Commerce Clause issue and found, on the basis of its opinion in the companion case of *National Can Corp. v. Department of Revenue*, 105 Wn.2d 327, 715 P.2d 128 (1986) (Appendix D, *infra*, p. D-1), that the B&O tax does not discriminate against interstate commerce. The court then found that there was a sufficient nexus between the State of Washington and activities performed on behalf of the Appellant to satisfy constitutional standards for purposes of the Commerce Clause and the Due Process Clause and also found that the tax was fairly apportioned (Appendix A, *infra*, pp. A-5 to A-9). Finally, the court rejected Appellant's argument regarding the Federal Interstate Income Tax Act concluding that the Washington B&O tax is not a "net income tax" within the meaning of the statute (Appendix A, *infra*, p. A-9).

## 2. Statement of Facts

Appellant is a corporation established under the laws of the State of Delaware that is qualified to do business in the State of Texas and maintains its principal place of business in Tyler, Texas. It is engaged in the business of selling pipe, plumbing and related products.

Appellant markets nationwide many types of plumbing pipes and fittings manufactured by its wholly-owned subsidiaries, Tyler Pipe Industries of Texas, Inc. ("Tyler-Texas"), Tyler Plastics Company, and others. The taxes for which refund is sought were assessed with respect to the gross receipts from sales by Appellant to Washington customers of products manufactured by the latter two named subsidiaries. Appellant and its subsidiaries are subject to, and pay, substantial franchise and *ad valorem* taxes in the State of Texas, both of which taxes are based in part upon the value of the products and the assets utilized in the production and storage of the products sold to Washington customers. Texas does not currently impose a net income tax or gross receipts tax.

Neither Appellant nor its subsidiaries maintain an office, plant, or any other place of business in the State of Washington. They are not qualified to do business in the State of Washington. They do not have any employees located in or active in the State of Washington, and they have never sent personnel into the State of Washington for the purpose of soliciting or accepting orders from customers. They do not send material or products into the State of Washington except by U.S. Mail or independent common carrier. They do not solicit sales in the State of Washington except through instrumentalities of interstate commerce, such as the telephone, advertisements in national trade magazines and occasional mailings from Tyler, Texas. Neither Appellant nor Tyler-Texas maintains any assets or inventory in the State of Washington. Accordingly, the Department of Revenue's sole basis for asserting taxing jurisdiction in this case is that Appellant's products

are handled in Washington by an independent sales representative, Ashe & Jones, Inc., which is located in Seattle. RP 15-19; RP 20-60.<sup>1</sup>

The sales representative acts independently of Appellant and its subsidiaries. It is paid on a commission basis according to the volume of sales of Appellant's products in its respective territories in the states of Washington, Oregon, Idaho, Montana and Alaska and in three Canadian provinces. It is not under the direct supervision or control of Appellant and does not receive any administrative and financial assistance or counseling from Appellant. The sales representative, on its own, solicits sales of Appellant's products, and also handles the plumbing products of various other firms and companies. RP 17; RP 268 *et seq.*

A typical sale is handled in the following manner. A potential customer, usually a wholesale plumbing or similar firm, contacts the sales representative with an order. The sales representative in turn contacts Appellant by telephone and forwards the order. All orders placed by a sales representative are subject to acceptance in Texas by Appellant. The products are shipped directly to the purchasing customer from Tyler, Texas, by common carrier, and the purchasing customer is billed by mailed invoice from Tyler, Texas. The customer pays Appellant directly; the sales representatives do not collect payments. Defective items are occasionally returned to Appellant via independent common carrier. In many cases, Washington customers contact Appellant directly by telephone or through the mail, bypassing the sales representative. In such a case the sales representative is not involved in the ordering process, and shipment and payment remain the same. RP 33 *et seq.*; RP 185 *et seq.*

---

<sup>1</sup>RP references are to the Report of Proceedings transcribed from the trial and made a part of the record on appeal in the Washington Supreme Court.

The market involved is primarily a national one. The advertising and the contacts usually made are on a national level. Although the independent sales representative does keep track of and advise on local market conditions, its activities are not necessary to enable Appellant to sell to Washington customers. RP 46 *et seq.*, RP 195 *et seq.*, RP 287.

During the audit period, neither Appellant nor its subsidiaries, sent any service personnel into the State of Washington. Thus, Appellant's only connection with the State of Washington was through the use of means of interstate commerce (i.e. telephone, mail and independent common carriers) and through the sales representative, who was independent of Appellant, handled the products of other companies, and was not involved in approximately 33% of the sales during the audit period. RP 17, 18, 19, 37, 38, 45, 268 *et seq.*

The State of Washington imposes the Washington B&O tax at the rate of .44% on gross receipts from the sale of products in the state. The state imposes the tax on the seller, not the buyer, of the items. The tax is described as a tax on the privilege of doing business in the state. R.C.W. Sections 82.04.220, 82.04.270, and 82.04.500. The tax is imposed separately on various activities performed within the state, including manufacturing and wholesaling. R.C.W. Sections 82.04.240 and 82.04.270. The taxes in issue in this case are entirely wholesaling taxes as Appellant performs no other taxable activities in the state. *Section 82.04.440 of the Revised Code of Washington provides an exemption from the manufacturing tax for taxpayers engaged in both manufacturing and wholesaling within the state who pay the wholesaling tax on products manufactured and then sold within the state. Therefore, despite the fact that the tax is imposed separately on each activity, the State of Washington imposes the same tax on persons who manufacture outside the state and wholesale within the state as it imposes on persons who both manufacture and wholesale within the state.*

## THE QUESTIONS ARE SUBSTANTIAL

The Washington Supreme Court erred grievously in deciding the case below. Despite the fact that two recent decisions of this Court, *Armco, Inc. v. Hardesty*, U.S. , 104 S.Ct. 2620, *rehearing denied*, U.S. , 105 S.Ct. 285 (1984) and *Maryland v. Louisiana*, 451 U.S. 725 (1981), set forth clear standards for assessing the unconstitutionality of a state taxing scheme that are applicable to the Washington B&O tax, the court below disregarded these standards. Instead, the court attempted to distinguish *Armco* and *Maryland* and reverted to earlier precedent of this Court and of the Washington Supreme Court to support its decision. *Armco* and *Maryland* have cast serious doubt on, if they have not in fact overruled, prior decisions involving the Washington B&O tax and raise substantial questions requiring plenary consideration by this Court of the issues raised below.

### I.

## THE WASHINGTON B&O TAX DISCRIMINATES AGAINST INTERSTATE COMMERCE.

The starting point of any analysis of a state tax is the decision in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, *rehearing denied*, 430 U.S. 976 (1977). There the Court stated that, in order to satisfy the constitutional requirements of the Commerce Clause (U.S. Constitution, Article I, Section 8, clause 3), a state tax must be applied to an activity with a substantial nexus with the taxing state, be fairly apportioned, not discriminate against interstate commerce, and be fairly related to the services provided by the state. Similarly, the Due Process Clause of the Fourteenth Amendment (U.S. Constitution, Amendment XIV, Section 1) requires that, for a state tax to be enforceable in interstate commerce, there be a minimal connection between the interstate activities of the taxpayer and the taxing state and a rational relationship between the income attributed to the state and the intra-

state value of the enterprise. *Mobil Oil Corp. v. Commissioner of Taxes of Vermont*, 445 U.S. 425, 436-437 (1980).

This Court has discussed the non-discrimination requirement in numerous cases and has held that any tax which by its terms or operation imposes greater burdens on out of state goods or activities than on competing in-state goods or activities must be struck down as discriminatory under the Commerce Clause. W. Hellerstein, "Constitutional Limitations on State Tax Exportation," 1982 *American Bar Fdn. Research J.* 1, 22 (1982). States are prohibited by the Commerce Clause from (1) granting a direct commercial advantage to local business under their taxing schemes, *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318, 328 (1977); *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 458 (1959); *Maryland v. Louisiana*, *supra*; or (2) subjecting interstate commerce to the risk of multiple tax burdens to which local commerce is not exposed, *Northwestern States Portland Cement Co. v. Minnesota*, *supra*; *Gwin, White & Prince, Inc. v. Henneford*, 305 U.S. 434 (1939).

The Washington statutory scheme unconstitutionally discriminates against out-of-state manufacturers such as Appellant who sell their products in Washington. Washington's B&O tax is imposed upon extraction of natural resources, manufacturing, retailing and wholesaling, at the rate of 0.44% on the value of products or the gross proceeds of sale. RCW 82.04.230, 82.04.240, 82.04.250, 82.04.270. A tax is imposed at the rate of 1% on the gross proceeds from service and other business activities. RCW 82.04.290. A Washington taxpayer who pays the tax on retailing or wholesaling is exempt from taxation of in-state manufacturing and extracting activities with respect to the items sold, and a Washington taxpayer who pays a manufacturing tax is exempt from taxation of in-state extraction activities with respect to the manufactured items. RCW 82.04.440. The effect of the Washington statute is to subject a Washington business to taxation only once on all of its extraction, manufacturing and whole-

sale or retail marketing activities, but to subject interstate business to double or triple taxation: full taxation in each separate state in which the out-of-state company conducts its extraction, its manufacturing or its wholesale or retail marketing activities.

The Washington B&O tax is at least as discriminatory as the taxing schemes held unconstitutional in *Armco, Inc. v. Hardesty*, *supra*, and *Maryland v. Louisiana*, *supra*. In *Armco*, an 8-1 majority of the Court held that the West Virginia wholesale gross receipts tax unconstitutionally discriminated against interstate commerce. Under the West Virginia tax scheme, a tax of 0.27% was imposed on wholesaling and a tax of 0.88% was imposed on manufacturing. West Virginia manufacturers paid only the manufacturing tax; they were exempted from the wholesaling tax. As a result, a company manufacturing and selling within West Virginia was subject to only one tax, whereas an out-of-state manufacturer was potentially subject to a tax on manufacturing in its home state and on wholesaling in West Virginia. The Court held that this taxing scheme discriminated against interstate commerce on its face and thus was invalid under the Commerce Clause.

The Washington B&O tax imposes the same rate of tax (.44%) on manufacturing and wholesaling activities, RCW 82.04.240 and RCW 82.04.270, but exempts from taxation the activities of in-state manufacturers with respect to items sold within the state. RCW 82.04.440. As a result, a company manufacturing and selling within Washington is subject to only one tax, and a company manufacturing out-of-state and selling within Washington is potentially subject to a tax in its home state on manufacturing and in Washington on selling. The Washington Supreme Court refused to apply *Armco* to invalidate the Washington B&O tax. *National Can Corp.*, *supra*, 715 P.2d at 131-135 (Appendix D, *infra*, pp. D-6 to D-13). Instead, the court purported to distinguish *Armco* on the ground that the Washington tax is not "facially discriminatory" and that the Washington taxes on manufactur-

ing and wholesaling are complementary and therefore compensatory. There is absolutely no rational basis for those conclusions, and the "distinction" between *Armco* and the instant case utterly fails to withstand scrutiny.

In a dissenting opinion in *General Motors Corporation v. Washington*, 377 U.S. 436, 451 (1964), which dissent was cited favorably in *Armco*, *supra*, U.S. at , 104 S.Ct. at 2623, Justice Goldberg discussed the difference between a tax scheme that grants a manufacturer an exemption from a wholesaling tax and one which grants a wholesaler an exemption from a manufacturing tax and stated that the latter "provision would seem to have essentially the same economic effect on interstate sales, but has the advantage of appearing nondiscriminatory." *General Motors Corporation v. Washington*, *supra*, 377 U.S. at 460. Justice Goldberg added that the resulting threat of multiple taxation to an out-of-state manufacturer would place him in a competitive disadvantage relative to an in-state manufacturer, resulting in a violation of the Commerce Clause. That the Washington B&O tax was the subject of his discussion is particularly noteworthy.

The Court's decision in *Maryland v. Louisiana*, *supra*, further undermines the conclusion of the court below that the Washington tax is not facially discriminatory. In *Maryland* the Court held that a "state tax must be assessed in light of its actual effect considered in conjunction with other provisions of a State's tax scheme." *Maryland v. Louisiana*, *supra*, 451 U.S. at 756. That holding served to invalidate a first use tax imposed by Louisiana on outer continental shelf gas brought into Louisiana for processing. The tax discriminated in favor of Louisiana residents because residents were granted credits against other state taxes for any payment of the first use tax on gas consumed in Louisiana while the first use tax was imposed without credits on any gas transported out of Louisiana after processing. The Court found that this scheme unquestionably discriminated against interstate commerce. Similarly, the Washington B&O tax, which purports to

treat all wholesalers equally by imposing a tax on gross receipts at the same rate for in-state and out-of-state manufacturers who sell in Washington, unquestionably discriminates against out-of-state manufacturers. The tax scheme accomplishes this by exempting in-state manufacturers from the manufacturing tax for items both manufactured and sold in Washington while out-of-state manufacturers are potentially subject to both a manufacturing tax in their state of manufacture and the Washington wholesaling tax.

The distinction observed by the Washington Supreme Court with respect to the manufacturing and wholesaling taxes being compensatory is even more suspect. The compensating tax issue was raised by the West Virginia Supreme Court of Appeals in *Armco* to justify the wholesaling exemption for West Virginia manufacturers since such manufacturers were subject to a higher tax than out-of-state manufacturers selling in West Virginia. This Court rejected that proposition because there was no basis for apportioning the higher manufacturing tax between manufacturing and wholesaling and because the manufacturing tax was not reduced for those companies that wholesale outside West Virginia. In this case, the wholesaling tax is the same for in-state and out-of-state manufacturers. Therefore, it is logically inconsistent to state that part of the wholesale tax is to compensate the state for the manufacturing tax which would otherwise be due from in-state manufacturers. Moreover, just as there was no reduction in the West Virginia manufacturing tax when wholesaling was done elsewhere, there is no reduction in the Washington wholesaling tax when manufacturing is done elsewhere. It is impossible to maintain that part of the wholesaling tax is in compensation for the exempted manufacturing tax. The Court in *Armco* also refused to consider manufacturing and wholesaling as "substantially equivalent events" such that the taxes on the two activities could be considered compensating as would, for instance, a sales tax and a use tax. There is absolutely no distinction on this score between *Armco* and the case at bar.

Furthermore, the Washington Supreme Court refused to apply the "internal consistency" rule of *Armco* that requires a court to determine the constitutionality of a tax based on the premise that the tax is imposed by every jurisdiction. Despite the fact that this Court rejected the contention that actual proof of discriminatory impact is required in order to find a tax invalid under the Commerce Clause, the court below stated that such proof will be required unless it could be shown that the tax in question was "facially discriminatory." While the internal consistency concept originated in the fair apportionment analysis of a multi-state net income tax case, this Court used the concept in *Armco* to invalidate a gross receipts tax and is applicable here. *Armco* did not require a *showing* of facial discrimination before applying the internal consistency rule, but merely an *allegation* of it. A court must make its determination of whether a tax discriminates on its face by assuming the tax is imposed in all states.

## II.

### THE WASHINGTON B&O TAX IS NOT FAIRLY APPORTIONED AND IS NOT FAIRLY RELATED TO SERVICES PROVIDED BY THE STATE.

In dealing with the fair apportionment and fairly related standards of the *Complete Auto* test, the court below similarly rejected controlling precedent of this Court. Apportionment is necessary to ensure that only income from intrastate activities is subjected to tax. While most apportionment questions have arisen in the context of state income taxes, the apportionment question is also significant in gross receipts tax cases, which present as great a danger of interference with interstate commerce because, as in this case, the total sales price of an item is subjected to tax despite the fact that a substantial part of the activity that resulted in that sale occurs outside the taxing jurisdiction. See the dissenting opinion of Justice Brennan in *General Motors Corp. v. Washington*, *supra*, 377 U.S. at 449-451. If each state in which activity re-

sulting in a sale occurred imposed a tax similar to the Washington B&O tax, the same gross receipts would be taxed two, three or more times. This Court's decision in *Armco* requires that a tax be fairly apportioned to reflect the business conducted in the state and requires the apportionment test to be conducted under the internal consistency concept. Based on the evidence presented below, the Washington B&O tax results in a tax out of all proportion to the business transacted by Appellant in the State of Washington because the greater portion of Appellant's gross receipts from sales in Washington results from activity in Texas rather than in Washington. Despite this fact, the Washington Supreme Court refused to apply the internal consistency test in determining whether the B&O tax is fairly apportioned.

The refusal of the court below to apply this Court's decision in *Armco, Inc. v. Hardesty*, *supra*, on substantial questions interpreting the United States Constitution calls for this Court to exercise plenary jurisdiction over this appeal.

## III.

### AS APPLIED TO APPELLANT, THE WASHINGTON B&O TAX IS UNCONSTITUTIONAL BECAUSE A SUFFICIENT NEXUS DOES NOT EXIST BETWEEN APPELLANT'S ACTIVITIES AND THE STATE.

The Washington Supreme Court also misconstrued this Court's decisions regarding whether or not a sufficient nexus between the State of Washington and Appellant's interstate activities exists. In holding that there were sufficient connections to impose the tax, the court below relied on the decisions in *Standard Pressed Steel Company v. Washington Department of Revenue*, 419 U.S. 560 (1975) and *Scripto, Inc. v. Carson*, 362 U.S. 207 (1960). Initially, it should be pointed out that *Scripto* involved the imposition of a use tax on an out-of-state seller, whereas the tax in question here is a gross receipts tax. This Court stated

in *Norton Company v. Department of Revenue of the State of Illinois*, 340 U.S. 534, 537 (1951), that cases involving use taxes are not controlling where the issue relates to a gross receipts tax because the presence of some local incident bringing the transaction within the taxing power of the state is more easily shown for a use tax. Thus, the activities performed in *Scripto* would not necessarily satisfy the nexus requirements for a gross receipts tax.

Although *Standard Pressed Steel* involved the same gross receipts tax that is at issue here, Appellant demonstrated at trial that the activities allegedly creating the required nexus were not of the same degree as those performed in *Standard Pressed Steel*, but were more similar to the activities performed in *National Bellas Hess, Inc. v. Department of Revenue*, 386 U.S. 753 (1967), *Norton Company v. Department of Revenue*, *supra*, and *McLeod v. J. E. Dilworth Company*, 322 U.S. 327 (1944). In *Standard Pressed Steel* the out-of-state manufacturer maintained a full-time salaried employee in the State of Washington whose duty it was to consult with a single important customer regarding its anticipated needs and requirements, encourage the purchase of products, design and test new products, and resolve product difficulties. The employee, an engineer, was assisted by a group of engineers who visited the customer from taxpayer's home office about every six weeks. In stark contrast to these activities, Appellant's only connections with the State of Washington were through interstate communications and transportation and through an independent sales representative. Appellant had no employees, inventory, manufacturing plants, sales offices, warehouses or property in the State of Washington. Its sales representative handled the products of many different companies, was not involved in substantial in-state solicitation and promotional activities and was not involved at all in many sales.<sup>2</sup> The courts

<sup>2</sup>Congress has specifically stated that this type of activity does not constitute the minimum connections necessary to subject a person to the taxing jurisdiction of a state for purposes of a net income tax. Federal

(Footnote continued on next page)

below, ignoring uncontradicted testimony that it was not necessary to utilize an independent sales representative either to make customers aware of Appellant's products or to make sales in the State of Washington, found that the activities of the sales representative constituted a sufficient connection between Appellant and the State of Washington to bring Appellant within the state's taxing power.

Additionally, the lower courts disregarded the uncontradicted evidence that fully one-third of Appellant's sales that were subjected to tax—sales of the utilities division—occurred with no participation whatsoever by the independent sales representative. According to this Court's holding in *Norton Company v. Department of Revenue*, *supra*, the utilities division sales are not taxable even if the activities of the sales representative created the required nexus to justify imposing the tax on sales handled by the representative. In *Norton* a Massachusetts-based company was taxed on all its sales in Illinois based on the presence in Chicago of a branch office and warehouse that made local sales. The company also made other sales in Illinois directly from its home office in Massachusetts. The Court found that, despite the company's own presence in the state—not just through an independent sales representative—Illinois could not tax the company on sales made directly from Massachusetts in which the Chicago office had no participation. Appellant urges that *Norton* supports a finding that none of Appellant's sales in Washington were taxable since Appellant had no presence in the state; however, at the very least, *Norton* requires that Appellant's utilities division sales are not

(Footnote continued from preceding page)

Interstate Income Tax Act, 15 U.S.C. Sections 381 *et seq.* Although this case involves a gross receipts tax, Congress' codification of minimal standards was spurred by its concern over the constitutional relationship between interstate commerce and the taxing power of individual states. Therefore, even if the Federal Interstate Income Tax Act is not applicable to a gross receipts tax, the standards set forth therein should be applicable under a constitutional analysis where the tax involved imposes as great a burden in interstate commerce as would a net income tax.

subject to the tax. The courts below refused to apply *Norton* and erroneously held that all sales were taxable.

Because of these unsupported and clearly erroneous findings, this Court must exercise its "power to examine the whole record to arrive at an independent judgment as to whether constitutional rights have been invaded. . . ." *Norton Company v. Department of Revenue, supra*, 340 U.S. at 538. This power constitutes a separate basis for exercising plenary jurisdiction, separate and apart from the questions raised above relating to the decision in *Armco*.

### CONCLUSION

For the foregoing reasons, the Court should note probable jurisdiction of this appeal.

NEIL J. O'BRIEN  
GARDERE & WYNNE  
1500 Diamond Shamrock Tower  
Dallas, Texas 75201  
(214) 979-4500

*Counsel for Appellant*

### IN THE SUPREME COURT OF THE STATE OF WASHINGTON

TYLER PIPE INDUSTRIES, INC.,  
a Delaware corporation,

*Appellant,*

v.

STATE OF WASHINGTON,  
DEPARTMENT OF REVENUE,

*Respondent.*

51110-1  
En Banc

DOLLIVER, C.J.—Tyler Pipe Industries, Inc. (Tyler Pipe) challenges a trial court ruling which upheld the constitutionality of Washington's business and occupation (B & O) tax against Tyler Pipe's commerce clause challenge. The trial court denied Tyler Pipe's request for a tax refund holding that the State had sufficient nexus to tax Tyler Pipe and that the federal interstate income tax act, 15 U.S.C. § 381 (1982), was inapplicable to Washington's B & O tax. We affirm the trial court.

The Washington Department of Revenue assessed B & O taxes against Tyler Pipe in the approximate amount of \$130,000 for its wholesaling activities in Washington. The tax, assessed pursuant to RCW 82.04.220 and .270, is on gross receipts from sales to Washington customers between January 1, 1976 and September 30, 1980 (the audit period).

Tyler Pipe obtained a preliminary injunction against collection of this tax which we reversed in *Tyler Pipe Indus., Inc. v. Department of Rev.*, 96 Wn.2d 785, 638 P.2d 1213 (1982). Tyler Pipe subsequently paid the taxes and filed this action for a refund. The trial court issued its memorandum opinion on June 15, 1984, denying Tyler Pipe's claim to a tax refund. A subsequent motion

for reconsideration was denied. On August 4, 1985, we accepted this case for review as a companion case with *National Can Corp. v. Department of Rev.*, Wn.2d , P.2d (1986).

## I

The facts, which were detailed by the trial court and for which there is substantial evidence (*Thorndike v. Hesperian Orchards, Inc.*, 54 Wn.2d 570, 343 P.2d 183 (1959)), are as follows:

Tyler Pipe is a Delaware corporation with its principal place of business in Tyler, Texas. Tyler Pipe markets, sells, and distributes cast iron, pressure and plastic pipe and fittings, and drainage products nationwide. Tyler Pipe owns several subsidiaries which manufacture and sell pipe and plumbing products. Tyler-Texas and Tyler Plastics are wholly-owned subsidiaries of Tyler Pipe. These two corporations manufacture the products sold by Tyler Pipe to Washington customers. All products sold in Washington are manufactured outside the state.

Tyler Pipe is organized into 4 divisions: marketing, purchasing and distribution, finance, and industrial relations. The marketing division consists of the drainage, waste, vent (DWV) sales department and the utility sales department. Tyler Pipe markets its products through these two departments. Most of Tyler Pipe's customers are wholesale distributors. In Washington, both departments use the same sales representative, Ashe and Jones, Inc. of Seattle.

The DWV sales department includes a cast iron DWV sales manager, three regional sales managers, and a Wade, Inc. (Wade) sales manager. Wade is a wholly-owned subsidiary of Tyler, marketing items auxiliary to a DWV plumbing piping system. Wade shares with Tyler a substantial number of the same officers and employees. Wade has its own Washington sales representative, Mechanical Agents, Inc. (MA) of Seattle, which main-

tains an inventory of Wade products (owned by Wade in MA's warehouse in Seattle).

Tyler's regional sales manager, Warren VanDerbeck, is responsible for all DWV (including Wade) sales in a region including Washington state. Tyler Pipe's sales representative for Washington state, Ashe and Jones, Inc., is a Washington corporation and handles all sales functions pertaining to its products in this state; however, both Tyler Pipe and Wade are represented in certain southern Washington counties by Bridgeport Sales, Ltd. of Portland, Oregon. For every sale made in Washington, a commission is paid to the appropriate sales representative even if the customer directly contacts Tyler Pipe or its subsidiaries about the sale.

Virtually all information received by Tyler Pipe, or any subsidiary, regarding the Washington market for Tyler Pipe products is communicated from the sales representatives. This information is necessary to keep Tyler Pipe competitive in the marketplace. The sales representatives regularly act on behalf of Tyler Pipe. In addition to their solicitations, the sales representatives handle approximately two-thirds of the orders to Tyler Pipe from Washington customers.

Tyler Pipe's Washington sales representatives perform any local activities necessary for maintenance of Tyler Pipe's market and protection of its interests because Tyler has no personnel designated as employees residing in Washington. The sales representatives are involved in all Tyler Pipe Washington sales transactions either actively or available to assist, if necessary. The sales functions of these representatives are essentially identical to those of the factory salesmen who represent Tyler in certain other parts of the country.

Neither Tyler Pipe nor any subsidiary paid to any other state any tax measured in whole or in part by sales in Washington, or

income resulting from those sales, during the audit period. Neither Tyler Pipe nor any subsidiary paid any real or personal property taxes in Washington during or for the audit period.

## II

The first issue is whether Washington's B & O tax discriminates against interstate commerce thereby violating the commerce clause of the United States Constitution. The four requirements for a valid state tax on interstate commerce under the commerce clause are as follows: (1) there must be a sufficient connection or nexus between the interstate activities and the taxing state; (2) the tax must be fairly apportioned; (3) the tax must not discriminate against interstate commerce; and (4) the tax must be fairly related to the services provided by the state. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279, 51 L. Ed. 2d 326, 97 S. Ct. 1076, *reh'g denied*, 430 U.S. 976 (1977). *Accord, Chicago Bridge & Iron Co. v. Department of Rev.*, 98 Wn.2d 814, 659 P.2d 463 (1983). The key factor in determining the constitutionality of Washington's B & O tax focuses on whether the tax discriminates against interstate commerce. As we held in the companion case of *National Can Corp. v. Department of Rev.*, Wn.2d , P.2d (1986), Washington's B & O tax does not discriminate against interstate commerce and the recent United States Supreme Court case of *Armco Inc. v. Hardesty*, U.S. , 81 L. Ed. 2d 540, 104 S. Ct. 2620, *reh'g denied*, U.S. , 83 L. Ed. 2d 222, 105 S. Ct. 285 (1984) is distinguishable.

## III

The key issue in this case and the basis of Tyler Pipe's challenge is whether its connections with the State of Washington were sufficient to satisfy constitutional standards for imposition of Washington's B & O tax under the due process and commerce clauses of the United States Constitution. Due process and com-

merce clause arguments are closely related, especially concerning the nexus issue, and will be considered together. *Chicago Bridge & Iron Co. v. Department of Rev.*, *supra* at 819.

The United States Supreme Court has held the due process clause of the Fourteenth Amendment imposes two requirements on a state before it can tax income generated in interstate commerce: (1) some minimal connection or "nexus" between the interstate activities and the taxing state and (2) a rational relation between the income attributed to the state and the intrastate value of the enterprise. *Mobil Oil Corp. v. Comm'r*, 445 U.S. 425, 436-37, 63 L. Ed. 2d 510, 100 S. Ct. 1223 (1980); *Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 57 L. Ed. 2d 197, 98 S. Ct. 2340 (1978).

The Department of Revenue has stated the requisite minimal connection or "nexus" in WAC 458-20-193B. See RCW 82.32.300. Under 193B, the crucial factor governing nexus is whether the activities performed in this state on behalf of the taxpayer are significantly associated with the taxpayer's ability to establish and maintain a market in this state for the sales.

This functional approach is in accord with *Standard Pressed Steel Co. v. Department of Rev.*, 419 U.S. 560, 42 L. Ed. 2d 719, 95 S. Ct. 706 (1975). In *Standard Pressed Steel*, the United States Supreme Court found a sufficient nexus for gross receipts tax when an out-of-state corporation had only one in-state employee. This employee had the responsibility of maintaining a relationship with the corporation's primary customer. No sales or orders were taken by the employee. The employee, however, regularly consulted with the customer regarding its needs for the manufactured product. The Supreme Court based its decision on the employee's activities which "made possible the realization and continuance of valuable contractual relations between" the corporation and its primary customer. *Standard Pressed Steel Co.*, at 562.

While not denying the activities of Tyler Pipe's sales representatives within this state helped it to establish and maintain its

Washington customers, Tyler Pipe claims that because these sales representatives are independent contractors, their activities should not be considered under a due process "nexus" test.

The United States Supreme Court has indicated the characterization of an in-state sales representative as an "independent contractor" is without constitutional significance with regard to the nexus issue. *Scripto, Inc. v. Carson*, 362 U.S. 207, 4 L. Ed. 2d 660, 80 S. Ct. 619 (1960). In *Scripto*, the Court determined that allowing the characterization of the taxpayer's in-state agent as an independent contractor to be a determining factor in whether a company would be taxed "would open the gates to a stampede of tax avoidance." *Scripto*, at 211. The test for nexus, the Court went on to say, should be simply the nature and extent of the agent's activities. *Scripto*, at 211. Cf. *Princess House, Inc. v. Department of Rev., State Bd. of Tax Appeals* order 18818 (Mar. 24, 1980) ("substantial nexus" found where out-of-state taxpayer was represented within the state by an independent manufacturer's representative paid on a commission basis).

The trial court's findings of fact, supported by substantial evidence in the record, reveal ample activities by the in-state sales representative which helped Tyler Pipe establish and maintain its market in this state. This is true even if its Washington based subsidiary (Wade) is not considered. Tyler Pipe challenges a number of the trial court's findings and conclusions concerning this issue. Tyler Pipe's challenges are without merit. Reviewing the entire record before us, we find substantial evidence to support each fact and conclusion entered by the trial court. See *Goodman v. Darden, Doman & Stafford Assocs.*, 100 Wn.2d 476, 670 P.2d 648 (1983). See also *Ridgeview Properties v. Starbuck*, 96 Wn.2d 716, 719, 638 P.2d 1231 (1982) (substantial evidence is evidence in sufficient quantum to persuade a reasonable person of the truth of the declared premise).

The sales representatives acted daily on behalf of Tyler Pipe in calling on its customers and soliciting orders. They have long-

established and valuable relationships with Tyler Pipe's customers. Through sales contacts, the representatives maintain and improve the name recognition, market share, goodwill, and individual customer relations of Tyler Pipe.

Tyler Pipe sells in a very competitive market in Washington. The sales representatives provide Tyler Pipe with virtually all their information regarding the Washington market, including: product performance; competing products; pricing, market conditions and trends; existing and upcoming construction products; customer financial liability; and other critical information of a local nature concerning Tyler Pipe's Washington market. The sales representatives in Washington have helped Tyler Pipe and have a special relationship to that corporation. The activities of Tyler Pipe's agents in Washington have been substantial.

The second prong under the due process test (and the second prong in the commerce clause analysis in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 51 L. Ed. 2d 326, 97 S. Ct. 1076, *reh'g denied*, 430 U.S. 976 (1977)) requires a rational relationship between the income attributed to the taxing state and the intrastate value of the enterprise. *Mobil Oil Corp. v. Comm'r*, 445 U.S. 425, 437, 63 L. Ed. 2d 510, 100 S. Ct. 1223 (1980). This test is met if the State's taxing formula is not arbitrary and does not tax the taxpayer "out of all appropriate proportion to the business transacted . . . in that State," *Exxon Corp. v. Department of Rev.*, 447 U.S. 207, 227, 65 L. Ed. 2d 66, 100 S. Ct. 2109 (1980) (quoting *Hans Rees' Sons, Inc. v. North Carolina ex rel. Maxwell*, 283 U.S. 123, 135, 75 L. Ed. 879, 51 S. Ct. 385 (1931)). The taxpayer has the burden of proving by clear and cogent evidence that the tax is in fact out of all appropriate proportion to the business transaction. *Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 274, 57 L. Ed. 2d 197, 98 S. Ct. 2340 (1978). The Supreme Court has refused to impose strict restraints on the State's taxing formula. *Moorman Mfg. Co.*, at 280.

Tyler Pipe cites *Hans Rees' Sons, Inc.* for the proposition that Washington's B & O tax is unconstitutional because it is out of all proportion to its activities in the state. The Court concluded in *Hans Rees' Sons, Inc.* that the State's formula was out of proportion when it produced a tax on approximately 80 percent of the taxpayer's income when only 17 percent of that income actually had its source in the state. *Hans Rees' Sons, Inc.*, at 135.

This case is not applicable. Not only does it deal with an entirely different tax scheme, but Washington's B & O tax does not approach the disparity of proportion found in the tax scheme in the *Hans Rees' Sons, Inc.* case. Also, the Supreme Court previously has upheld Washington's B & O tax on entire gross receipts from sales made by the taxpayer into Washington state. *Standard Pressed Steel Co. v. Department of Rev.*, 419 U.S. 560, 42 L. Ed. 2d 719, 95 S. Ct. 706 (1975). Because the receipts from sales made to other states were not included in the taxpayer's taxable gross receipts, the Court concluded that the tax was "apportioned exactly to the activities taxed . . ." *Standard Pressed Steel Co.*, at 564. See also *Chicago Bridge & Iron Co. v. Department of Rev.*, 98 Wn.2d 814, 830, 659 P.2d 463 (1983) (Washington's B & O tax is inherently proportional to in-state activities). A rational relationship and not a strict, exact formula is all that is necessary under the due process and commerce clauses. *Moorman Mfg. Co.*, at 280.

The State has not attempted to tax any sales transactions other than those involving Washington customers. Tyler Pipe urges that any receipts earned from sales from its utility division or from sales of orders placed directly to it from its Washington customers should be exempted from Washington's B & O tax. In its memorandum opinion, the trial court found no useful distinction between the utility division and the DWV division of Tyler Pipe for the purposes of taxing its sales within this state. This is supported by the findings of fact and the record. We concur with the holding of the trial court that the tax, as levied by the State, was

in proportion to Tyler's in-state activity. We affirm the trial court's finding of sufficient nexus between Tyler Pipe and the State of Washington.

#### IV

The State raises the issue of Tyler Pipe's standing for the first time on appeal. Standing was not an issue at the trial level. If the issue of standing is not submitted to the trial court, it may not be considered on appeal. *Baker v. Baker*, 91 Wn.2d 482, 484, 588 P.2d 1164 (1979). See RAP 2.5(a). We refuse to review the issue of standing.

Finally, Tyler Pipe raises the issue of whether the federal interstate income tax act, 15 U.S.C. §§ 381, *et seq.* (1982), exempts Tyler Pipe from Washington's B & O tax. This argument is without merit. The federal statute applies only to a "net income tax"; Washington's B & O tax is not a net income tax or a net tax on anything. Rather, "B & O taxes are for the privilege of engaging in business during a certain time frame, measured by applying a rate of tax to some tax base." *Puyallup v. Pacific Northwest Bell Tel. Co.*, 98 Wn.2d 443, 451, 656 P.2d 1035 (1982).

The trial court is affirmed.

WE CONCUR:

---

---

---

---

---

---

---

---

---

---

IN THE SUPERIOR COURT OF THE  
STATE OF WASHINGTON

IN AND FOR THE COUNTY OF THURSTON

TYLER PIPE INDUSTRIES, INC.,  
a Delaware corporation,

*Plaintiff,*

vs.

STATE OF WASHINGTON,  
DEPARTMENT OF REVENUE,

*Defendant.*

No. 81-2-00731-4

MEMORANDUM  
OPINION

Plaintiff has urged this court to grant a refund of the B & O tax which it has paid pursuant to RCW 82.04.220 and 270. Plaintiff bases its request on the argument that Washington's B & O tax as applied to the plaintiff here violates the Due Process Clause and the Commerce Clause of the United States Constitution. Furthermore, the plaintiff argues that the Federal Interstate Income Tax Act prohibits applying the Washington B & O tax to Tyler Pipe's sales to Washington customers.

After closely examining the plaintiffs' arguments, this court must conclude that the Washington B & O tax as applied to Tyler Pipe does not violate the Constitution under either a due process challenge or a commerce clause challenge. Nor does the Federal Interstate Income Tax Act prohibit the imposition of this tax on Tyler Pipe.

**DUE PROCESS**

The Due Process Clause requires first, that there be a minimum connection or "nexus" between the taxing state and the interstate activities of the taxpayer. Relevant to the determination of whether or not the requisite "minimal connection" exists is

whether and to what extent the person taxed has used the services, benefits, and protections provided by the taxing state; that is, "whether the state has given anything for which it can ask return." Secondly, there must exist a rational relationship between the income attributed to the taxing state and the intrastate value of the enterprise.

The requisite "minimal connection" or "nexus" has been elaborated in WAC 458-20-193B. Under Rule 193B, the key factor governing nexus is the functional analysis of whether the activities performed in this state on behalf of the taxpayer are significantly associated with the taxpayer's ability to establish and maintain a market in this state for the sales.

In agreement with this functional approach adopted by the Washington legislature, the Supreme Court of Washington and the United States Supreme Court have held that the intrastate activity is a taxable "nexus" where it helps to establish and maintain a market for the sale of products in the state. *Standard Pressed Steel v. Department of Revenue*, 419 U.S. 560, 42 L.Ed. 2d 719, 95 S. Ct. 706 (1975).

Following legislative directive and legal precedent, this court must examine the activities of the sales representatives of Tyler Pipe within this state to determine whether or not their activities helped Tyler Pipe to establish and maintain its Washington customers. After thoroughly reviewing these activities, this court finds that the activities of the sales representatives clearly helped Tyler Pipe establish and maintain its market in this state. Nor is there any useful distinction between the Utility Division and the DWV Division of Tyler Pipe for the purposes of taxing its sales within this state.

The sales representatives acted daily on behalf of Tyler Pipe in calling on the trade and soliciting orders. They are the channel for approximately two-thirds of the customer orders to Tyler Pipe.

(Interrogatory #25-2) Through their sales contacts, the representatives have long established relations with Tyler Pipe's customers through which they maintain and improve the name, recognition, market share and goodwill of Tyler Pipe. (Defendant's first Interrogatory; plaintiffs answers: Interrogatory #33, p.27.) Through their relationships in the trade, the representatives are also able to relay customer feedback to Tyler Pipe regarding customers, (See Interrogatory #30-2, p.23), market trends, (see Interrogatory #30-2, p.23), product performance, customer financial reliability (See deposition of James B. Horan, p.13. See also, Representative's Contract with Tyler Pipe,) and other "critical" information of a local nature. The representatives are, in fact, Tyler Pipe's only source of information about Washington market conditions, such conditions being vital to keeping Tyler Pipe competitive within the marketplace. (See 12/8/78 memo to Ashe & Jones from Bob Clendennon of Tyler Pipe. See also Interrogatory #30-2, p.28) To the extent local activities are necessary for maintenance of Tyler's market and protection of its interests, those activities are performed by the representatives since Tyler has no regular employees in the State. Tyler Pipe utilized the sales representatives to persuade local Washington engineers and contractors to specify Tyler products in their projects. (See Interrogatory #30, p.27) Although the Washington representatives are not actively involved in pricing or servicing Tyler's products, they are involved in all the sales transactions in the passive sense of being present, aware of Tyler Pipe's transactions and available to assist if necessary. The sales representatives afford to Tyler's customers the "presence" of Tyler as they stand by at all times to assist the customers, to encourage product sales and to promote generally the good will of Tyler Pipe.

In addition to customer relations, the sales representatives supply Tyler Pipe with vital feedback associated with competitor's product lines in the Washington area, potential new customers, and are the first line evaluators of the financial responsibility of potential new customers. (See representatives' agreement.)

Additionally, the representatives sometimes become involved in handling complaints and occasionally make inquiries for Tyler Pipe regarding late payments. (See Deposition of James B. Horan, p.11) Tyler Pipe's sales representatives in Washington are assisted by Tyler agents by telephone approximately once a month per agent. (See Interrogatory #28, p.25)

Finally, Tyler uses Washington roads and transportation facilities whenever it sells a product for delivery to a Washington customer. Services provided by the state also include police and fire protections, "utility" contracts with local governments, the availability of the courts and numerous other advantages of a civilized society.

As a result of the activities of Tyler Pipe's representatives on behalf of Tyler Pipe and as a result of the benefits made possible to Tyler Pipe arising from these activities, this court finds that a sufficient "nexus" exists between the state of Washington and the activities to legitimately assess the Washington B & O tax on Tyler Pipe's sales to its Washington customers.

The second prong of the two prong test for the due process challenge is that there must exist a "rational relationship between the income attributed to the taxing state and the intrastate value of the enterprise." *Chicago Bridge and Iron Company v. Department of Revenue*, 98 Wn.2d 814, 659 P.2d 463 (1983), *U.S. App. Pndg. (C.B.I.)*. As stated in *C.B.I.*, "no such tax is assessed against interstate sales to other states. Hence the tax is *inherently proportional to in-state activities*. *C.B.I.* p. 830. (emphasis added) The State of Washington has not attempted to tax any other sales transactions *other* than those involving Washington customers. Although the tax may be imprecise, the Constitution requires a rational relationship, not exact precision. *C.B.I.*, p. 830. The tax, as levied by the State, is inherently proportional to Tyler's in-state activity.

## COMMERCE CLAUSE

The commerce clause requires the taxing state to meet a four prong test: (1) there must be a sufficient connection or nexus between the interstate activities and the taxing state; (2) the tax must be fairly apportioned; (3) the tax must not discriminate against interstate commerce; and (4) the tax must be fairly related to the services provided by the state. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 278-82, 51 L.Ed. 2d 326, 97 S. Ct. 1076 (1977).

The first and second part of the commerce clause test have already been discussed in the court's analysis of the due process challenge and need not be repeated here. Specifically, there is a sufficient "nexus" based on the activities of Tyler Pipe's sales representatives to justify the Washington B & O tax. Secondly, the tax is based on only Washington sales and is therefore inherently proportional to the State of Washington.

The third prong of the commerce clause test requires that a state tax does not discriminate against interstate commerce. That is not to say that a tax may not impose a burden on interstate commerce for the commerce clause does not shelter interstate commerce from "paying its way." The Supreme Court of Washington has stated in *C.B.I., supra*, at 830:

"A state tax on interstate commerce is not discriminatory unless it affords a 'differential tax treatment of interstate and intrastate commerce.' Washington's tax treats intrastate and interstate businesses equally, making no distinction between them. See RCW 82.04. Both . . . are taxed only once on their gross proceeds, not separately for each transaction as manufacturer, wholesaler, or retailer.

The Washington Supreme Court also rejected the argument that the *risk* of double taxation (i.e., taxation where the product is manufactured and taxation where the product is sold) is sufficient grounds for declaring the tax unconstitutional. *C.B.I., supra*, at

p.831. The commerce clause does not prohibit overlaps in taxation nor does it require exact precision in taxation. Therefore, because the Washington B & O tax is applied equally to intra-state activities as well as to interstate activities, it cannot be found to discriminate against interstate commerce.

The fourth and final consideration under the commerce clause test requires the tax to be fairly related to services provided by the state. Again, the Supreme Court of Washington offers this court guidance in addressing this requirement. In *C.B.I., supra*, that court stated that the fourth requirement is closely connected to the first prong of the commerce clause test, the nexus requirement. "It requires that the measure of the tax be tied to the earnings which the State . . . has made possible." *Id.* at 832. Clearly, Tyler Pipe benefits from the presence of police and fire protection, the availability of the courts, "utility" contracts with local governments, the use of Washington roads and transportation facilities and numerous other "advantages of a civilized society." Therefore, the activities carried on in the state of Washington by Tyler Pipe's sales representatives benefit Tyler Pipe and the tax being assessed is tied to these benefits and earnings which the State has made possible. As a result of the analysis under the four prong test of *Complete Auto Transit, supra*, this court concludes the Washington B & O tax is constitutionally valid.

#### FEDERAL INTERSTATE INCOME TAX ACT

The FIITA does not, it seems to this court, apply to the B & O tax which the state has attempted to collect from the taxpayer.

Dated this 15 day of June, 1984, at Olympia, Washington.

---

CAROL A. FULLER, JUDGE

### IN THE SUPERIOR COURT OF THE STATE OF WASHINGTON IN AND FOR THE COUNTY OF THURSTON

TYLER PIPE INDUSTRIES, INC.,  
a Delaware corporation,

*Plaintiff,*

vs.

STATE OF WASHINGTON,  
DEPARTMENT OF REVENUE,

*Defendant.*

No. 81-2-00731-4

FINDINGS OF  
FACT,  
CONCLUSIONS  
OF LAW, AND  
JUDGMENT

This matter was tried to the Court beginning on November 21, 1983. The plaintiff taxpayer, Tyler Pipe Industries, Inc. [Tyler Pipe or Tyler], was represented by Thomas C. McKinnon of Cartano, Botzer, Larson & Birkholz. The defendant State of Washington Department of Revenue [the department] was represented by the Attorney General, through Assistant Attorney General James R. Tuttle. Closing arguments were continued to December 16, 1983. After certain supplemental briefing requested by the Court, the Court issued its Memorandum Opinion, dated June 15, 1984, denying plaintiff's claim to a tax refund. A subsequent Motion for Reconsideration by plaintiff was denied, following argument thereon, by Memorandum Opinion of the Court dated August 6, 1984.

KENNETH O. EIKENBERRY  
Attorney General  
State of Washington  
James R. Tuttle  
Assistant Attorney General  
Department of Revenue  
415 General Admin. Bldg. AX-02  
Olympia, Washington 98504  
(206) 753-5528

The Court has heard and considered the oral testimony of witnesses and the written and oral arguments of counsel. In addition, the Court has reviewed and considered the exhibits admitted at trial and the published depositions of Manley Hendricks, James B. Horan, Glenn H. Jones, Dale Meador, and Warren VanDerbeck, together with the remainder of the record herein. Being now fully informed in the matter, the Court enters the following:

### FINDINGS OF FACT

1. Tyler Pipe seeks a refund of "wholesaling" business and occupation taxes it has paid, measured by its sales in Washington State during the period from January 1, 1976 through September 30, 1980 (the audit period), in the total amount (including post-assessment interest) of \$130,010.56, plus statutory interest and costs if any are authorized. No refund of taxes measured by Wade, Inc. sales (see below) is sought. The following findings cover the audit period.

2. Tyler Pipe is incorporated in Delaware, has its principal place of business in Tyler, Texas and is in the business of selling piping, plumbing and related products. Virtually all of the products it sells are manufactured in Tyler, Texas. Its organization consists of four divisions: marketing, purchasing and distribution, finance, and industrial relations. The marketing division, in turn, consists of the DWV (drainage, waste, vent) sales department and the utility sales department.

3. The customers of the DWV sales department generally are wholesale plumbing supply distributors (jobbers), whose own customers in turn are "mechanical" and/or "plumbing" contractors. The customers of the utility sales department generally are wholesale "waterworks" distributors, who in turn sell to "utility" contractors, cities, etc. In Washington, both departments use the same sales representative, Ashe and Jones, Inc. of Seattle.

4. The DWV sales department includes a cast iron—DWV sales manager, a Wade sales manager, and three regional sales managers. Wade Inc., a wholly-owned subsidiary of Tyler, markets items auxiliary to a DWV plumbing piping system. It functions as a subdivision of the DWV Sales Department because of its commonality with the DWV products. Like the rest of the DWV sales department, Wade's customers are plumbing wholesalers. Wade, Inc. shares with Tyler a substantial number of the same officers and employees. Wade has its own Washington sales representative, Mechanical Agents, Inc. (MA) of Seattle, which maintains an inventory of Wade products (owned by Wade) in MA's warehouse in Seattle.

5. Tyler's regional sales manager covering the territory of which Washington state is a part, Warren VanDerbeck, is responsible for all DWV (including Wade) sales. He visits, coordinates with, instructs, and assists both Washington sales representatives, Ashe and Jones and Mechanical Agents.

6. Tyler Pipe's sales representatives for Washington State, Ashe and Jones and Mechanical Agents, are Washington corporations and handle all sales functions pertaining to its products in this state. For every sale made in Washington, a commission is paid to the sales representative in whose territory the customer is located, even if the customer itself directly contacts Tyler Pipe or its subsidiaries about the sale.

7. The sales representatives have long-established and valuable relationships with Tyler Pipe's customers. Through their sales contacts, the representatives maintain and improve the name recognition, market share, goodwill, and individual customer relations of Tyler Pipe.

8. Virtually all information received by Tyler Pipe or any subsidiary, concerning the Washington market for Tyler Pipe products, is communicated orally from the sales representatives.

Such information includes vital feedback about existing and potential new customers, product performance, competing products, pricing, market conditions and trends, existing and upcoming construction projects, customer financial reliability, and other critical information of a local nature concerning Tyler Pipe's Washington market. Such information, provided on a regular, timely basis, is necessary to keeping Tyler Pipe competitive in the marketplace.

9. The sales representatives act regularly on behalf of Tyler Pipe in calling on the trade generally and soliciting specific orders from wholesalers. During the audit period, out of a total of 11,438 orders placed with Tyler (including Wade) for delivery in Washington, 7,628 orders were received and transmitted to Tyler by the Washington sales representatives. Thus, in addition to their solicitations the sales representatives actually physically handle approximately two-thirds of the orders to Tyler Pipe from Washington customers.

10. To the extent local activities are necessary for maintenance of Tyler Pipe's market and protection of its interests, those activities are performed by the sales representatives, since Tyler has no personnel designated as employees residing in Washington. For example, the sales representatives make "secondary calls" to persuade Washington architects and engineers, and plumbing contractors (customers of the wholesale distributors), to specify and use Tyler products in their projects; the representatives also provide price quotations of Tyler Pipe products for specific construction projects. They may be asked by Tyler to make inquiries about specific competing products and to provide counteracting sales information. Sales representatives participate in investigating and handling adjustments for, or complaints from, customers. Finally, the local sales representative may make inquiries for Tyler regarding late payments; although this has not been much of a problem in Washington, it is Tyler's usual practice to involve

the local representative in trying to obtain payment from a slow-paying customer before that account is referred to an outside agency for collection.

11. The sales representatives are involved in *all* Tyler Pipe Washington sales transactions either actively, as set forth above, or at least in the passive sense of being present, aware of the transactions, and available to assist if necessary. The sales representatives afford to Tyler's customers the "presence" of Tyler as they stand by at all times to assist the customers, to encourage product sales, and to promote generally the goodwill of Tyler Pipe.

12. The aforementioned sales functions of Tyler's Washington sales representatives are essentially identical to those of the factory salesmen who represent Tyler in certain other parts of the country. There are no significant differences between these sales representatives and those salespersons with regard to how they solicit and process orders or otherwise "call on the trade," although only the salespersons are designated by Tyler as employees.

13. A typical sales transaction is processed as follows. The local sales representative having received an order, or the customer, calls Tyler and conveys the order to a telephone sales correspondent in the appropriate division. During the audit period, neither Tyler Pipe nor any subsidiary ever rejected an offer or order arranged or transmitted by a Washington sales representative.

14. An invoice is prepared at Tyler on a pre-printed form bearing the name "Tyler Pipe Industries" and the company's logo, with the division name being added by the computer. The invoice form identifies Tyler Pipe Industries, Inc. as the seller, and the same invoice form is used for billing by all divisions. The transaction is basically the same when the sale is made from Wade stock stored in the warehouse of the local sales representative (*e.g.*, Mechanical Agents).

15. Tyler goods are sold F.O.B. destination. Title to the goods passes to the customer at the point of delivery, *i.e.*, in Washington State for the sales in question. Tyler Pipe, as shipper, is responsible for paying freight, delivery, and other shipping costs. Shipments to customers are made, either directly from Tyler's plant in Tyler, Texas via commercial motor freight or, in the case of Wade sales, from Mechanical Agents' Seattle warehouse by commercial carrier. Tyler Pipe's total sales to Washington customers during the audit period consisted of \$24,919,708 thus shipped from Texas and \$787,736 of Wade products thus shipped from the Seattle warehouse. (Minimal amounts of Wade products also were shipped to Washington customers from an out-of-state location during the audit period.)

16. For all sales made by Tyler Pipe or any subsidiary or division, the customer's payment is made directly to Tyler Pipe at the same post office box in Dallas, Texas.

17. Neither Tyler Pipe nor any subsidiary paid to any other state any tax measured in whole or in part by sales in Washington, or income resulting from those sales, during the audit period. Neither Tyler Pipe nor any subsidiary paid any real or personal property taxes in Washington during or for the audit period.

18. Tyler Pipe takes advantage of and uses Washington roads and transportation facilities whenever it sells a product for delivery to a Washington customer. Other benefits provided to Tyler Pipe and its products by the state of Washington include police and fire protections, "utility" construction contracts awarded by local governments which utilize Tyler products, the availability of the courts, and numerous other advantages of a civilized society.

### CONCLUSIONS OF LAW

1. This Court has jurisdiction over the subject matter and the parties in this case.

2. The test applied to state taxation of interstate business under the due process clause of the U.S. Constitution is two-pronged: (1) there must be a "minimal connection" or "nexus" between the interstate activities and the taxing state, and (2) the income attributed to the state for tax purposes must be rationally related to "values connected with the taxing state." Both parts of this test are met here.

3. The department has duly promulgated WAC 458-20-193B (Rule 193B) defining the conditions of liability for payment of business and occupation tax by persons selling goods originating in other states to buyers in Washington. That rule is valid.

4. The actions of Tyler Pipe through its representatives in Washington create a sufficient nexus to satisfy the first prong of the due process test, as interpreted in Rule 193B, and thus permit application of the wholesaling business and occupation tax for sales made by Tyler Pipe in Washington. These actions constitute "local activity which is significantly associated with the seller's ability to establish and maintain a market in this state for [its] sales." The representatives' "instate services enable [Tyler Pipe] to make the sales." Orders for the goods sold in Washington are solicited in this state by an agent or other representative of Tyler Pipe, the seller. Moreover, Tyler Pipe's Washington sales representatives perform significant services in Washington which contribute to the establishment and maintenance of the market and otherwise enable Tyler Pipe to make sales within the state. The fact that Tyler designates them as representatives, rather than as employee salesmen, without a difference in function, lacks constitutional significance.

5. The second prong of the due process test is also satisfied here because the sales proceeds, the measure of the tax, are rationally related to values connected with Washington. Since no Washington business and occupation tax is assessed against sales made by Tyler Pipe in other states, the tax imposed on sales in Washington is inherently proportioned to in-state activities.

6. The commerce clause of the U.S. Constitution imposes four requirements for a state tax on interstate commerce: (1) there must be a sufficient connection or nexus between the interstate activities and the taxing state; (2) the tax must be fairly apportioned; (3) the tax must not discriminate against interstate commerce; and (4) the tax must be fairly related to the services provided by the state. Those requirements are met here.

7. The commerce clause nexus requirement in the context of this case is the same as the due process nexus requirement discussed above, Conclusion of Law No. 4, and thus is met here.

8. The Washington business and occupation tax, as imposed on Tyler Pipe's sales in Washington, is fairly apportioned. The tax was assessed upon Tyler Pipe's gross proceeds from Washington sales only, not its total volume of interstate sales. Thus, the tax was and is apportioned exactly to the activities taxed.

9. The Washington business and occupation tax, as applied to Tyler Pipe, does not discriminate against interstate commerce. Both intrastate and interstate businesses are treated equally. Tyler Pipe, other out-of-state and in-state manufacturers, and other businesses, selling at wholesale in Washington, are subject to wholesaling business and occupation tax at the same rate. Under such circumstances, Tyler Pipe is not discriminated against merely because it can speculate about the "risk" of multiple taxation, when in fact no other state taxes its Washington sales.

10. The Washington business and occupation tax imposed on Tyler Pipe is fairly related to services provided it by the state. Tyler Pipe receives numerous benefits from the state of Washington.

11. The Washington business and occupation tax is not a "net income tax" for purposes of Public Law 86-272, codified as 15 U.S.C. §§ 381 et seq. It is neither an "income" tax nor a "net" income tax, as defined in that statute. Since the effect of Public Law 86-272 is expressly limited to a net income tax, that statute is inapplicable here.

### JUDGMENT

On the basis of the foregoing Findings of Fact and Conclusions of Law, IT IS HEREBY ORDERED, ADJUDGED AND DECREED that:

1. The plaintiff's claim to a refund of excise taxes paid is denied and dismissed with prejudice;
2. Judgment is granted to the defendant State of Washington Department of Revenue; and
3. The defendant is awarded its taxable costs herein.

DATED this 24th day of October, 1984.

---

CAROL A. FULLER  
Judge of the Superior Court

Presented by:

KENNETH O. EIKENBERRY  
Attorney General

By \_\_\_\_\_  
James R. Tuttle  
Assistant Attorney General  
Attorneys for Defendant

Approved As To Form:

CARTANO, BOTZER, LARSON & BIRKHOLZ

By \_\_\_\_\_  
Thomas C. McKinnon  
Attorneys for Plaintiff

JOHN SPELLMAN  
Governor

GLENN R. PASCALL  
Director

STATE OF WASHINGTON  
DEPARTMENT OF REVENUE  
*Olympia, Washington 98504 MS-AX-02*

March 12, 1981

Cartano, Botzer and Chapman DETERMINATION  
1300 IBM Building No. 81-39  
Seattle, Washington 98101

Attention: Thomas A. Sterken Re: Tyler Pipe Industries, Inc.  
Registration No. C600 382 582  
Tax Assessment No. 0719800

Dear Mr. Sterken:

We have thoroughly reviewed your petition of February 25, 1981, on behalf of the above referenced taxpayer. It seeks a correction of Tax Assessment No. 0719800 which was issued in the amount of \$123,159 on December 26, 1980 covering the audit period from January 1, 1976 through September 30, 1980. The assessment represents a tax and interest deficiency under the business and occupation tax classification, Wholesaling-Other, measured by the taxpayer's gross income from its sales of pipe and plumbing fittings to wholesale customers in Washington State. The assessment is unpaid.

The taxpayer protests the tax assessment as being an unconstitutional application of WAC 458-20-193B (Rule 193B) under the facts outlined in the petition, in violation of the Interstate Commerce and Due Process clauses of the Federal Constitution. The petition sets forth, in detail, the taxpayer's legal arguments and the case law supports relied upon.

Our analysis of the petition reveals that no useful purpose would be served the taxpayer or the state of Washington by scheduling a hearing of these matters. The Department of Revenue has fully and uniformly stated its position, under the law, on the precise factual and constitutional questions presented in this case, as set forth below. The Department is committed in litigation to the position that Rule 193B requires payment of the tax under the facts here present. Accordingly, pursuant to WAC 458-20-100(7), the taxpayer's petition is hereby denied.

To put the Department's position in perspective, we will restate here the facts of this case as presented in the taxpayer's petition and undisputed by the auditor.

The only connection which the Company has had with the State of Washington during the tax years in question, as described in detail below, is that *the Company has sold plumbing fittings and pipe to Washington customers*. The products which the Company distributes and sells are actually manufactured by two of the Company's wholly-owned subsidiaries, Wade, Inc. ("Wade"), (a Virginia corporation) and Tyler Pipe Industries of Texas, Inc. ("Tyler Pipe"), (a Texas corporation), both of which maintain their principal offices and places of business in Tyler, Texas. Wade manufactures special order plumbing fittings, while Tyler Pipe manufactures most other types of plumbing pipes and fittings. Neither the Company nor their subsidiaries maintain any employees or offices in the State of Washington nor is any of such companies qualified to do business in the state. *Orders are placed with the Company through the Company's independent sales representatives in the State of Washington*. Ashe & Jones of Seattle represents the Company in part of the state as well as in certain other states and handles Tyler Pipe products, while Mechanical Agents, Inc., also of Seattle, represents the Company in another part of the State of Washington and in certain other states and handles Wade products. Neither the Company, which is the seller, nor Tyler Pipe has any assets or inventory in the

State of Washington. *Wade maintains only a small inventory at Mechanical Agents, Inc.'s Seattle warehouse.*

The *Company's sales representatives* act independently and receive commissions on sales made to customers in their territory, but their duties are very limited. Neither representative actively solicits business for the Company and both representatives also handle the plumbing products of numerous other firms and companies. The representatives' customers consist primarily of various wholesale plumbing outfits. *The representatives provide service manuals to customers in the State of Washington*, but catalogs and price lists are mailed directly to customers by the Company from Tyler, Texas.

Most, but not all sales to Washington residents are handled through a sales representative. Some orders, however, are placed directly by the customer with the Company. A typical sale made through a representative is handled in this manner. *First, a representative's customer indicates its plumbing needs to a Seattle representative. The representative then either calls the Company in Texas and gets a telephone bid from the Company, or checks the Company's price list, and calls the Company to place an order with a telephone sales correspondent.* Assuming Company approval of the order, the representative sends the Company a confirming purchase order and the Company fills the order. All sales of Tyler Pipe products and most sales of Wade products are shipped by the Company from the Company's facilities in Tyler, Texas to customers in Washington by common carriers. An invoice is prepared to bill the customer after any goods are shipped. The invoices printed at the Company bear the Tyler Pipe/Tyler Corporation logo. For the relatively small portion of sales made from *Wade's inventory stored in Mechanical Agents' Seattle warehouse*, the transaction is basically the same. Mechanical Agents must obtain the approval of the Company before a shipment is made out of such inventory.

Customer's payments are made directly to the Company; its representatives never handle any such payments nor do the representatives assist the Company in any way in collecting any overdue amounts. Full payment is due after delivery to the customer with various cash discounts allowed to encourage prompt payment. The Company has never used the Washington court system to collect any delinquent accounts in Washington, nor availed itself of any other Washington services.

In the event of a customer complaint, *the customer either calls the Company or one of the representatives who then refers the customer to the Company.* The Company has never sent any service personnel to the State of Washington, as all valid complaints are resolved by phone or correspondence with the Company, either by crediting the customer's account or by return and replacement of any defective pipes or fittings. (Emphasis ours.)

It is the firm position of the Department that instate activities of sales representatives precisely such as those underscored in the taxpayer's stipulated presentation above constitute nexus upon which Washington State may constitutionally predicate its taxing jurisdiction over gross sales income here. The Department, the Washington State Board of Tax Appeals, and the Washington Courts have sustained the imposition of this taxing jurisdiction in cases such as this after full consideration of the very case law precedents cited in the taxpayer's petition.

The Superior Court for Thurston County sustained the Department's position on October 2, 1980 in PVO International, Inc. v Department of Revenue, Cause No. 79-2-00732-1. The Court expressly upheld the validity of Rule 193B and held further that,

For the purpose of determining the existence of nexus under the due process and commerce clause of the U.S. Constitution, there is no constitutional significance to be

assigned to the label used to describe the relationships between PVO and Raymer Brand or between PVO and M & S, whether the labels be "employee" or "independent contractor" or "broker". (These were independent brokers who represented PVO and others. PVO had no employees here.) (Parenthetical inclusion ours.)

Representatives' activities, even short of order taking or sales solicitation, conducted in this state on behalf of out-of-state sellers which result in sales to Washington customers constitute nexus for business tax on such sales. This is the import of the Rule 193B statement,

... the following activities are examples of sufficient local nexus for application of the business and occupation tax:

...

- 4 The delivery of the goods is made by a local outlet or from a local *stock of goods* of the seller in this state.
- 5 Where an out-of-state seller, either directly or by an agent or other representative, *performs significant services in relation to establishment and maintenance of sales* into the state, the business tax is applicable, even though (a) the seller may not have formal sales offices in Washington or (b) the agent or representative may not be formally characterized as a "salesman". (Emphasis ours.)

Actual hard sell solicitation is not a criteria or a threshold requirement for a finding of nexus. Rule 193B speaks in terms of "activity . . . significantly associated in any way with the seller's ability to establish and maintain a market" and "significant services in relation to establishment and maintenance of sales into the state". In the General Motors case our State Supreme Court spoke of whether "the tax bore a reasonable relation to . . . activ-

ities within the State" and when that case went on up, the U.S. Supreme Court spoke of whether the "tax is levied on incidents of a substantial local business in Washington", whether the "activities, i.e., the local incidents . . . may be fairly related to those activities", whether there were "substantial services . . . with relation to the establishment and maintenance of sales", and whether the "local activities . . . form some definite link, some minimum connection".

The terms significant, reasonably related, substantial, fairly related, definite link, and minimum connection may not be susceptible of a precise definition for application in every case. Indeed, most out-of-state sellers who do business in Washington through the efforts of brokers, agents, or sales representatives urge the conclusion that the activities engaged in here are minimal, insignificant, insubstantial, and of a mere public relations and goodwill ambassadorial nature. However, we are not persuaded that the acts of providing service manuals and taking and transmitting sales orders for a company which maintains a stock of goods here, however small, are insignificant in establishing and maintaining a sales market here. Surely, to use the kind of language employed by the court in *Standard Pressed Steel Company v Washington*, 419 US 560 (1975) these activities "make possible the realization and continuance of valuable contractual relations"—namely, the sales made thereby. The taxpayer's only business is sales. If the activities of its instate representatives did not stimulate and maintain sales, the taxpayer would not pay commissions. In any event if the taxpayer doubts that the activities of its local representatives significantly affect sales, the taxpayer is always in the position to weigh the rate of commission paid (or total costs to it for services rendered by its independent contractors) against the rate of the Washington business tax (currently .0044) and make the business decision of whether it wishes to have sales related activities performed in its behalf by persons in this state.

Rule 193B is a codification of the collective rationale of numerous U.S. Supreme Court decisions, including *Norton Company v Illinois Department of Revenue*, 340 US 534 (1951); *General Motors v Washington*, 377 US 436 (1964); and *Standard Pressed Steel Company v Washington*, *supra*. We will not here discuss the debatable claimed factual distinctions between the taxpayer's activities and those dealt with in the many cases cited in its petition, including the cases referenced above. As a matter of constitutional principle such factual differences are simply not dispositive of the taxpayer's liability. They have been considered and rejected. See *Princess House, Inc. v State*, Board of Tax Appeals Docket No. 18818 (March 24, 1980); *United Grocers, Inc. and Northwest Grocery Company v State*, BTA Docket No. 80-6 (November 25, 1980); and *PVO International Co. v Department of Revenue*, *supra*.

Finally, the Department of Revenue, over many years of excise tax administration, has successfully held that 15 USC 381 (commonly referred to as Public Law 86-272) is not applicable to gross receipts taxes, even when challenged by the very arguments raised in the taxpayer's petition. See *Clairol, Inc. v Kingsley*, 270 A2d 702 (1970) dismissed for want of a substantial Federal question, 28 L Ed 2d 643 (1971). The Federal act, by its very terms, applies only to taxes on or measured by net income, and has no effect on excise taxes measured by gross income. Gross receipts taxes, assuming nexus requirements are satisfied, as here, have been permitted for the last 40 years when imposed by the destination state and prohibited when imposed by the state of origin of the goods. Cf. *Hellerstein*, *State Taxation of Interstate Business and the Supreme Court*, 62 Va Law Review 149 (1976).

For all of the foregoing reasons the taxpayer's petition; on the merits, is hereby denied. Tax Assessment No. 0719800 has accrued mandatory extension interest of \$2,425, for a total of

C-8

\$125,584, which is due for payment within twenty days from the date of this Determination.

Very truly yours,

STATE OF WASHINGTON  
DEPARTMENT OF REVENUE  
INTERPRETATION AND  
APPEALS DIVISION

---

Edward L. Faker, Hearing Officer

cc: Tyler Pipe Industries, Inc.

C-9

JOHN SPELLMAN  
Governor

GLENN R. PASCALL  
Director

STATE OF WASHINGTON  
DEPARTMENT OF REVENUE  
*Olympia, Washington 98504 MS-AX-02*

April 30, 1981

Cartano, Botzer and Chapman FINAL DETERMINATION  
1300 IBM Building No. 81-39A  
Seattle, Washington 98101  
Attention: Thomas A. Sterken Re: Tyler Pipe Industries, Inc.  
Registration No. C600 382 582  
Tax Assessment No. 0719800

Dear Mr. Sterken:

Your appeal petition of March 31, 1981 to the Director of the Department of Revenue seeks to have Determination 81-39 set aside. The Determination was issued on March 12, 1981 without a hearing. It sets forth the facts and issues pertinent to the taxpayer's appeal covering an audit period from January 1, 1976 through September 30, 1980. Those facts and audit details will not be repeated here.

The taxpayer's current petition is simply a copy of the original petition which presented the taxpayer's position and cited case law supports for that position. Our review of Determination 81-39 reveals that it fully and properly represents the position of the Department of Revenue, under the prevailing case law and Revenue Rule 193B. The taxpayer's repetition of its arguments merely serves as an expression that it disagrees with the Department's position. No new or different arguments are proffered. Thus, it

clearly appears that no useful purpose would be served the taxpayer or the state of Washington by scheduling in an oral hearing of these matters. Further debate of the legal issues and constitutional authorities is unnecessary. Accordingly, the taxpayer's request for a hearing before the Director is hereby denied.

On the merits, Determination 81-39 sets forth the position of the Department which has been uniformly applied in cases such as this throughout many years of tax administration. In short, the most meaningful and significant activity engaged in here by the taxpayer's two selling entities, Tyler Pipe and Wade, Inc., is the sales related activity, including some solicitation, by "representatives" resident in this state, albeit they are independent agents. As Determination 81-39 explains, this fact alone—representatives performing significant services in relation to establishment and maintenance of sales—is sufficient to constitute nexus and gives this state jurisdiction to tax gross sales into Washington. It is fruitless to further debate whether the activities are significant or insignificant or whether the case law relied upon may be distinguishable in some factual patterns from the taxpayer's activities here. The simple facts are that the taxpayer's instate representatives do some soliciting, do forward and facilitate orders for goods, and do otherwise generally represent the taxpayer's interests in the Washington State sales market. It is patent that the most significant activity a seller can perform concerning a sale is getting the order. We simply cannot accept the taxpayer's position which argues, in essence, that it would pay commissions to sales agents here who perform no significant function.

We refer again to Determination 81-39, which is incorporated herein by this reference, as having fully responded to the taxpayer's petition arguments. It properly presents the position of the Department of Revenue in the face of the very constitutional tax challenges argued here. We concur with its findings and conclusions. Accordingly, the taxpayer's petition is denied.

Tax Assessment No. 0719800 has accrued additional extension interest of \$3,795, for a total of \$126,954, which is due for payment within twenty days from the date of this Final Determination.

Very truly yours,

STATE OF WASHINGTON  
DEPARTMENT OF REVENUE

---

S. Ed Tveden, Assistant Director

cc: Tyler Pipe Industries, Inc.

IN THE SUPREME COURT  
OF THE STATE OF WASHINGTON

NATIONAL CAN CORPORATION,  
KALAMA CHEMICAL, INC., and  
XEROX CORPORATION,

*Appellants,*

v.

STATE OF WASHINGTON,  
DEPARTMENT OF REVENUE,

*Respondent.*

No. 51910-2  
En Banc

UTTER, J.—This is a direct appeal from the trial court where various commercial enterprises (Taxpayers) claimed Washington's multiple activities exemption to the business and occupation (B&O) tax, RCW 82.04.440, discriminates against interstate commerce in violation of the commerce clause, U.S. Const. art. 1, § 8. The trial court ruled there was no unlawful discrimination. We agree and hold for the respondent, Department of Revenue (Department), that the challenged exemption does not violate the commerce clause. Our holding makes it unnecessary to reach the other issues raised by the parties concerning the constitutionality of both the tax refund interest provision, RCW 82.32.060, and the proposed legislation, ESSB, 3678, as well as the appropriate form of relief to be afforded Taxpayers.

Fifty-three separate actions for refunds of B&O taxes paid to the Department were filed. Each Taxpayer claimed the tax violates the commerce clause. These actions were joined for decision by the Thurston County Superior Court which granted the Department's motion for summary judgment and denied the Taxpayers' motions for injunctions against further collection of the

B&O taxes in question. The 53 cases were consolidated for this appeal and, in addition, 52 other substantially similar actions are pending in Thurston County Superior Court. The amount in question is estimated to exceed \$423 million.

Three plaintiffs were selected by the parties to serve as "test cases" in the appeal. Kalama Chemical, Inc., a representative plaintiff, manufactures its products in Washington and sells them outside of Washington. Xerox Corporation, the second representative plaintiff, manufactures its products outside Washington and sells them within Washington. The appellant in a companion case would appear to fit most closely within this category of plaintiffs. *See Tyler Pipe Indus., Inc. v. Department of Rev.*, Wn.2d , P.2d (1986). National Can Corporation, the third representative plaintiff, manufactures products in Washington for sale outside Washington, and also manufactures products outside Washington for sale in Washington. Kalama Chemical, Inc. seeks a refund of the manufacturing tax it paid (\$495,000); Xerox Corporation seeks a refund of the wholesale tax it paid (\$1.5 million); National Can Corporation seeks a refund of both the manufacturing and wholesale taxes it paid (approximately \$900,000). The period in dispute is from 1980 to the present.

The issue before us is whether Washington's B&O tax exemption, RCW 82.04.440, violates the commerce clause because it (1) discriminates against interstate commerce, (2) is unfairly apportioned, or (3) is not fairly related to the services provided by the state.

Neither this court, nor the state Legislature, "is the final arbiter" of commerce clause issues. *See Southern Pac. Co. v. Arizona ex rel. Sullivan*, 325 U.S. 761, 89 L. Ed. 1915, 65 S. Ct. 1515 (1945). In an earlier challenge to this B&O tax, we recognized "our duty [is] to abide by controlling United States Supreme Court decisions construing the federal constitution." *Association of Washington Stevedoring Cos. v. Department of*

*Rev.*, 88 Wn.2d 315, 318, 559 P.2d 997 (1977); *Department of Rev. v. Association of Wash. Stevedoring Cos.*, 435 U.S. 734, 55 L. Ed. 2d 682, 98 S. Ct. 1388 (1978). This court's rulings on the constitutionality of the Washington B&O tax have generally withstood the United States Supreme Court's scrutiny, *see, e.g., General Motors Corp. v. Washington*, 377 U.S. 436, 12 L. Ed. 2d 430, 84 S. Ct. 1564 (1963); *Standard Pressed Steel Co. v. Department of Rev.*, 419 U.S. 560, 42 L. Ed. 2d 719, 95 S. Ct. 706 (1975), except when we have read the commerce clause too broadly and struck down the tax. *See Association of Washington Stevedoring Cos. v. Department of Rev.*, 88 Wn.2d at 318-20.

We find ourselves today in a similar situation. For over 30 years, Washington's B&O tax has been repeatedly upheld by the federal courts against charges that it discriminated against interstate commerce. *See B.F. Goodrich Co. v. State*, 38 Wn.2d 663, 231 P.2d 325, *cert. denied*, 342 U.S. 876, 96 L. Ed. 659, 72 S. Ct. 167 (1951). In *B.F. Goodrich*, we held that the B&O tax does not discriminate against interstate commerce because, under that law, all wholesalers are taxed identically. We relied on the theory that any multiple-tax burdens on interstate commerce, whereby out-of-state businesses must pay a manufacturing tax in another state plus a wholesale tax in Washington, were merely "an inevitable consequence of the power of the several states to tax". 38 Wn.2d at 669; *see also General Motors Corp. v. State*, 60 Wn.2d 862, 376 P.2d 843 (1962) (B&O tax upheld against charges of discrimination, applying the *Goodrich* analysis). The Supreme Court affirmed, *General Motors Corp. v. Washington*, 377 U.S. 436, 12 L. Ed. 2d 430, 84 S. Ct. 1564 (1964), but specifically declined to pass on the question of discrimination in the form of multiple-tax burdens because the appellant there failed to demonstrate any actual multiple-tax burden by showing that another state levied an equivalent tax.

In *Chicago Bridge & Iron Co. v. Department of Rev.*, 98 Wn.2d 814, 832, 659 P.2d 463 (1983), this court upheld the tax against

charges of discrimination in the form of multiple-tax burdens. The court cited *Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 277 n.12, 57 L. Ed. 2d 197, 98 S. Ct. 2340 (1978), for the proposition that the multiple-tax burdens experienced by interstate businesses are a "consequence of the combined effect of different states' laws" and were not caused by Washington's taxing scheme. 98 Wn.2d at 832. The United States Supreme Court dismissed the subsequent appeal "for want of a federal question," *Chicago Bridge & Iron Co. v. Washington Dept. of Rev.*, 464 U.S. 1013, 78 L. Ed. 2d 718, 104 S. Ct. 542 (1983), which we understand to be a decision on the merits. *Washington v. Confederated Bands and Tribes of the Yakima Indian Nation*, 439 U.S. 463, 476 n.19, 58 L. Ed. 2d 740, 99 S. Ct. 740, *reh'g denied*, 440 U.S. 940, 59 L. Ed. 2d 500, 99 S. Ct. 1290 (1979).

Taxpayers assert, however, that a recent Supreme Court case, *Armco, Inc. v. Hardesty*, U.S. , 81 L. Ed. 2d 540, 104 S. Ct. 2620 (1984),<sup>1</sup> effectively overrules, *sub silentio*, these 30 years of Supreme Court doctrine. As a result of their reading of *Armco*, Taxpayers ask this court to strike down the state's B&O tax and refund all monies allegedly improperly received under it since 1980.

Due to factual differences between the West Virginia tax, challenged in *Armco*, see 104 S. Ct. at 2621-22, and the Washington

<sup>1</sup>The decision has already provoked considerable comment. See Judson & Duffy, *An Opportunity Missed: Armco, Inc. v. Hardesty, A Retreat from Economic Reality in Analysis of State Taxes*, 87 W. Va. L. Rev. 723 (1985); Lathrop, *Armco—A Narrow and Puzzling Test for Discriminatory State Taxes Under the Commerce Clause*, Taxes 551 (August 1985); Lightburn & McArthur, *U.S. Supreme Court Ignores Unitary Issue in Armco, Inc. Opting for Discriminatory Finding*, 3 J. of St. Tax'n 211 (1984); Note, *A Call for Internal Consistency Among State Taxing Schemes: Armco, Inc. v. Hardesty*, 38 Tax Lawyer 519 (1985); *Sup. Ct. Holds West Virginia's Wholesale Gross Receipts Tax Unconstitutional*, The Tax Adviser 487 (August 1984); *West Virginia Gross Receipts Tax Discriminates Against Interstate Commerce*, 3 J. of St. Tax'n 143 (1984).

tax, we do not believe the United States Supreme Court is requiring us to forge new commerce clause doctrine and disregard earlier decisions not overruled. We are unable to find such a command in the *Armco* decision. We are also troubled by the "free-rider" effect of Taxpayers' argument. As Taxpayers conceded at oral argument, their interpretation of *Armco* would force the State to forego taxing a substantial number of in-state transactions where state services had admittedly been furnished. This implies that a state, to make up the deficit, must impose a double tax burden on in-state manufacturer-wholesalers.

### *The Commerce Clause Issues*

RCW 82.04.220 imposes, in general, a tax upon the privilege of engaging in business activities in Washington. The tax is measured by the application of rates against (1) the value of the products, (2) gross proceeds of sales, or (3) the gross income of the business, whichever is applicable. RCW 82.04.240 imposes a tax upon Washington manufacturers. RCW 82.04.270 taxes every person who sells products at wholesale in Washington. The disputed provision, RCW 82.04.440, provides that persons taxable under RCW 82.04.270 (wholesalers) shall not be taxed under RCW 82.04.240 (as local manufacturers). Thus, local manufacturers who wholesale their products strictly in Washington pay only the wholesaling tax. Further, a local extractor of a product who wholesales in Washington pays only the wholesaling tax, just as do out-of-state extractors. RCW 82.04.440. Under RCW 82.04.240, in-state manufacturers and extractors who sell their products out of state, pay only the manufacturing tax, at a rate substantially identical to that paid by in-state wholesalers.

A state B&O tax must pass a 4-prong test to be valid under the commerce clause: (1) There must be a sufficient *nexus* or connection between the taxing state and the business taxes; (2) the tax must be *fairly apportioned*; (3) the tax cannot *discriminate* against interstate commerce in favor of local commerce; and (4)

the tax must be *fairly related* to the services provided by the taxing state. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279, 51 L. Ed. 2d 326, 97 S. Ct. 1076 (1977). *Department of Rev. v. Association of Washington Stevedoring Cos.*, 435 U.S. 734, 55 L. Ed. 2d 682, 98 S. Ct. 1388 (1978). Appellants contend that Washington's B&O tax fails the last three prongs of this test. Because the heart of Taxpayers' complaint is that the statute fails the third prong, discrimination, that issue is addressed first. The second (fairly apportioned) and fourth (fairly related) prongs will be addressed together. Nexus is not at issue in this case, but is contested in the companion case. See *Tyler Pipe Indus., Inc. v. Department of Rev.*, \_\_\_ Wn. 2d \_\_\_, \_\_\_ P.2d \_\_\_ (1986).

#### A. Discrimination.

A state's taxing scheme is discriminatory under the commerce clause if it grants a direct commercial advantage to local businesses or subjects interstate commerce to a risk of multiple tax burdens, to which strictly local commerce is not exposed. See *Boston Stock Exch. v. State Tax Comm'n*, 429 U.S. 318, 50 L. Ed. 2d 514, 97 S. Ct. 599 (1977); *Gwin, White & Prince, Inc. v. Henneford*, 305 U.S. 434, 83 L. Ed. 272, 59 S. Ct. 325 (1939). Any direct commercial advantage to local businesses inherent in Washington's B&O tax results from duplicative tax burdens; e.g., the fact that strictly local businesses pay only one tax (either wholesale or manufacturing), while interstate businesses may possibly be subjected to one tax in this state and another tax at a different level of distribution in another state. Appellants contend that the recent Supreme Court decision, *Armco, Inc. v. Hardesty*, \_\_\_ U.S. \_\_\_, 81 L. Ed. 2d 540, 104 S. Ct. 2620 (1984), controls where there is a possibility of multiple-tax burdens and requires the invalidation of Washington's B&O tax.

In *Armco*, the Court invalidated West Virginia's gross receipts tax, under which local manufacturers were exempted from payment of the wholesale tax when they sold their locally-manu-

factured products in West Virginia. Out-of-state manufacturers were required to pay the West Virginia wholesale tax when they sold their products in that state.

West Virginia's gross receipts tax is claimed to be the mirror-image of Washington's present tax. West Virginia granted strictly local manufacturer-wholesalers an exemption from its wholesale tax; Washington grants strictly local manufacturer-wholesalers an exemption from its manufacturing tax. Besides providing an exemption to taxpayers who have already paid one state excise tax, the two tax systems are similar in that they are gross receipts taxes.<sup>2</sup> Their points of difference, however, have become more noteworthy after the *Armco* decision. The West Virginia tax exacted substantially different tax rates on manufacturing (.27 percent) and wholesaling activities (.88 percent), which precluded the Court from finding that the wholesaling tax compensated for the manufacturing tax. *Armco*, 104 S. Ct. at 2623. By exacting substantially identical rates (.44 percent) for each activity, the Washington tax does not present the same obstacle to finding the taxes are compensatory.

In *Armco*, the Court held that West Virginia's tax facially discriminated against interstate commerce, 104 S. Ct. at 2622, because it provided that "two companies selling . . . property at wholesale . . . will be treated differently depending on whether the taxpayer conducts manufacturing in the State or out of it." *Armco*, 104 S. Ct. at 2622-23. The Court further determined that under the West Virginia tax scheme the manufacturing and wholesaling were not "substantially equivalent events" which would allow for the imposition of compensating taxes. *Armco*,

<sup>2</sup>The similarities were acknowledged by the Department when it was before the *Armco* Court. See Brief of Amicus, *Armco*, 104 S. Ct. at 2624. In oral argument before this court, however, the Department stated that the *Armco* opinion, with its emphasis on the rates and measures of the West Virginia tax, makes the differences between the two states' taxes more significant than their similarities.

104 S. Ct. at 2623. It also noted that West Virginia did not allow for a proportionate reduction of its manufacturing tax when the manufactured goods were sold out of state, but did allow such a reduction when the goods were partly manufactured out of state. This was taken as evidence that the manufacturing tax was "not in part a proxy for the gross receipts tax imposed on Armco . . ." 104 S. Ct. at 2623.

While the Court did not explain what it meant by "substantially equivalent events,"<sup>3</sup> its reliance on *Maryland v. Louisiana*, 451 U.S. 725, 758-60, 68 L. Ed. 2d 576, 101 S. Ct. 2114 (1981), indicates a criteria to guide us in determining when the selling and wholesaling taxes would be deemed compensatory and therefore substantially equivalent. In *Maryland v. Louisiana*, *supra*, Louisiana claimed its first-use tax compensated for a severance tax the state had imposed on local natural gas production. The first use tax fell primarily on gas produced in the federal Outer Continental Shelf (OCS) and piped to Louisiana processing plants, before being distributed to out-of-state consumers. The Court stated the 2-pronged criteria for determining compensatory taxes: (1) both taxes must be designed to meet the same ends; (2) local and interstate taxpayers similarly situated must receive equal treatment. 451 U.S. at 758-59.

The Louisiana tax failed on both prongs of the test. The purpose of the severance tax was to protect Louisiana's natural resources and compensate for their depletion. The first-use tax, however, could not be designed for that same purpose, "since Louisiana has no sovereign interest in being compensated for the severance of resources from the federally owned OCS land." 451

<sup>3</sup>That the rate varies slightly for various types of businesses, is not germane to the present issue. The variance comes from a subsequently enacted surtax. RCW 82.04.2904. Moreover, mathematical equality is not required. *General American Tank Car Corp. v. Day*, 270 U.S. 367, 373, 70 L. Ed. 635, 46 S. Ct. 234 (1926).

U.S. at 759. The Court also noted that Louisiana's first-use tax directly altered market forces in three impermissible ways: (1) certain local uses of OCS gas were exempted from the tax; (2) its credit system encouraged "natural gas owners involved in the production of OCS gas to invest in mineral exploration and development within Louisiana" rather than continue to pursue out-of-state, *e.g.*, OCS, development; (3) the credit system also assured that in-state end users of OCS gas would be insulated from the cost increases resulting from the first use tax. 451 U.S. at 757.

None of the skewed market behavior due to the Louisiana tax appears to have developed in West Virginia. The *Armco* Court, however, found that the lack of symmetry in the West Virginia tax structure demonstrated that the selling and manufacturing taxes did not share the same end. 104 S. Ct. at 2623. That West Virginia apportioned its manufacturing tax according to the percentage of in-state manufacturing a particular product represented, meant that West Virginia's selling tax could not be a substantially equivalent event for the manufacturing tax. In contrast, however, the flat rate character of the Washington taxes evidence the Legislature's intent to treat the two taxes as complementary and, therefore, compensatory.

Furthermore, the Washington B&O tax does not exhibit the infirmities that led the Court in *Maryland v. Louisiana*, *supra*, to conclude the first-use tax could not be a compensatory tax for the state's severance tax. The Washington B&O tax is designed to tax the privilege of engaging in business activity *within* the state. RCW 82.04.220. Both the selling and the manufacturing taxes are exacted to address the same state burdens attendant on granting such a privilege. All who engage in selling activity within Washington pay the selling B&O tax, while those in-state manufacturers who sell out-of-state are taxed on their manufacturing activity. Each Taxpayer is taxed only once, at a substantially

uniform rate,<sup>4</sup> unlike West Virginia, for the privilege of doing business in Washington.

Nor does the tax exhibit a discriminatory impact. Unlike the Louisiana tax, the market forces are not altered by the incidence of the tax. In-state manufacturers selling out-of-state do not gain a tax advantage by shifting sales of their product to the local market. Similarly, out-of-state manufacturers selling in-state gain no tax advantage by moving their manufacturing operations in state. Also in contrast with the Louisiana tax is the fact that in-state consumers are not insulated from the price effects of the tax on the goods.

We are further persuaded that the Washington tax is valid because it is conceptually identical to the pre-1968 New York stock transfer tax the Court endorsed in *Boston Stock Exchange v. State Tax Comm'n*, 429 U.S. 318, 50 L. Ed. 2d 514, 97 S. Ct. 599 (1977) which was in turn reaffirmed in *Armco*, 104 S. Ct. at 2622. *Boston Stock Exchange* involved New York's attempt to keep the New York Stock Exchange by amending the stock transfer tax so that non-residents who completed transfers entirely in New York paid a lower tax than would residents, and that transfers occurring entirely within New York could only be taxed to a maximum of \$300, while there was no ceiling on other transfers. The tax was patently discriminatory and, unlike the B&O tax, was not part of a larger tax structure. The Court, however, spoke favorably of the unamended statute that taxed residents and nonresidents alike on one of several taxable stock transactions that could occur within the state. For both kinds of taxpayers, "the occasion of the tax was the occurrence of at least

<sup>4</sup>By way of example, the Court did suggest that sale and use taxes fell on substantially equivalent events. Other than representing activities farther downstream in the distribution chain, we do not see an economically significant difference between "sale and use" and "manufacturing and sale." *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 51 L. Ed. 2d 326, 97 S. Ct. 1076 (1977), requires some relationship between a legal distinction and "economic realities." 430 U.S. at 279.

one taxable event in the State, the rate of tax was based solely on the price of the securities, and the total tax was determined by the number of shares sold." 429 U.S. at 322-23.

The *Armco* Court relied heavily upon the *Boston Stock Exchange* case as authority for striking down the West Virginia tax. *Boston Stock Exchange's* favorable treatment of the pre-1968 amendments, see 429 U.S. at 330, and the apparent centrality of that holding to *Armco* requires harmonization of the two opinions. The incongruities between Taxpayers' reading of *Armco* and earlier, well-established commerce clause cases, see, e.g., *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 69 L. Ed. 2d 884, 101 S. Ct. 2946 (1981); *Complete Auto*, *supra*; *Boston Stock Exchange*, *supra*, makes us reluctant to extend *Armco* as Taxpayers urge. There is a disturbing formalism in their argument that manufacturing and wholesaling are never "substantially equivalent events." To read *Armco* thusly would foreclose analyzing a taxpayer's burden in light of both the structure of the relevant tax system and its effect on a single economic unit. Appellants' argument would force us to regard the gross receipts tax system as consisting of two separate taxes, manufacturing and selling, and to retreat from the *Complete Auto* "practical effects" test which *Armco* does not overrule or claim to modify. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. at 274. To do so would be to ignore the "economic realities," 430 U.S. at 279, that a business unit frequently operates at several levels in the distribution chain and the costs of those various operations come to bear on the single product which serves as the measure of taxation. See also *Judson & Duffy*, 87 W. Va. L. Rev. at 741; *Lathrop*, *Taxes* at 552, 559.

Similarly, to avoid other incongruities posed by Taxpayers' arguments, we do not read *Armco* as requiring that the "internal consistency" requirement be applied to determine discrimination. The concept, "internal consistency," originated in the fair apportionment analysis of a multi-state net income tax case, *Container*

*Corp. of Am. v. Franchise Tax Bd.*, 463 U.S. 159, 169, 77 L. Ed. 2d 545, 103 S. Ct. 2933 (1983), and its applicability to gross receipts tax cases has been questioned. See Lathrop, Taxes at 557. Nevertheless, the concept seems to have been used only to determine whether Armco, Inc. had to show actual harm once it had demonstrated the tax provision was facially discriminatory. See Judson & Duffy, 87 W. Va. L. Rev. at 739. As we have previously discussed, however, Washington's tax is not facially discriminatory. We note further that the Court, were it to have grafted the concept onto the discrimination prong, would have obscured the *Complete Auto* test by treating the "multiple taxation" apportionment prong as a discrimination problem. Reflecting its greater complexity, the "fair apportionment" prong has been subject to more generous standards than has the discrimination prong. See, e.g., *Container Corp.*, 463 U.S. at 170; *Moorman Mfg. v. Bair*, 437 U.S. 267, 278, 57 L. Ed. 2d 197, 98 S. Ct. 2340 (1978).

Because the West Virginia and Washington taxes differ significantly, we must reject appellants' argument and rely on the long history of the United States Supreme Court's treatment of this state's gross receipts tax as having withstood commerce clause challenges, see *Department of Rev. v. Association of Washington Stevedoring Cos.*, 435 U.S. 734, 55 L. Ed. 2d 682, 98 S. Ct. 1388 (1978); *Standard Pressed Steel Co. v. Department of Rev.*, 419 U.S. 560, 42 L. Ed. 2d 719, 95 S. Ct. 706 (1975); *General Motors Corp. v. Washington*, 377 U.S. 436, 12 L. Ed. 2d 430, 84 S. Ct. 1564 (1964); *Chicago Bridge & Iron Co. v. Department of Rev.*, 98 Wn.2d 814, 659 P.2d 463 (1983); *Crown Zellerbach Corp. v. State*, 45 Wn.2d 749, 278 P.2d 305 (1954); *B.F. Goodrich Co. v. State*, 38 Wn.2d 663, 231 P.2d 325, cert. denied, 342 U.S. 876, 96 L. Ed. 659, 72 S. Ct. 167 (1951), as well as the general development of commerce clause analysis from *Complete Auto* to *Armco*. See, e.g., *Container Corp. of America v. Franchise Tax Bd.*, *supra*; *Commonwealth Edison Co. v. Montana*,

*supra*; *Maryland v. Louisiana*, *supra*; *Moorman Mfg. Co. v. Bair*, *supra*. Under these two lines of precedent, we do not find the tax discriminatory.

#### B. Fair Apportionment; Tax Fairly Related to Services Provided by the State.

Taxpayers also claim that Washington's B&O tax violates the commerce clause because it is not fairly apportioned to reflect the amount of business conducted here, and it is not fairly related to the services rendered by Washington. As a result, Taxpayers complain that they are unfairly taxed upon more than 100 percent of their incomes. Hence, under the second and fourth prongs of the *Complete Auto* test, Taxpayers claim that interstate businesses are improperly subjected to multiple-tax burdens.

##### 1. Fair apportionment.

Most apportionment cases have arisen in challenges to state income taxes where the income of a unitary multi-state business comes from a variety of tax jurisdictions. As Judson and Duffy note, a B&O tax on business activity within the state does not present the same difficulty in determining a nexus between business activity and the tax jurisdiction. Judson & Duffy, 87 W. Va. L. Rev. at 728. Moreover, even in the income tax cases, the Court has afforded legislatures a generous standard. In *Exxon Corp. v. Wisconsin Dept. of Rev.*, 447 U.S. 207, 219-20, 65 L. Ed. 2d 66, 100 S. Ct. 2109 (1980), the Court looked only to whether there was "a rational relationship between the income attributed to the State and the intrastate values of the enterprise." See also, e.g., *Container Corp. of Am. v. Franchise Tax Bd.*, *supra*. Earlier, the *Moorman* Court had refused to require Iowa to employ the favored 3-factor test, urged here by Taxpayers, instead of its single-factor test for apportioning interstate commerce income. To disturb the formula, the taxpayers in *Moorman* would have to show by "clear and cogent evidence" that the income attributed to the State is in fact "out of all appropriate proportions to the busi-

ness transacted . . . in that State' . . . or has 'led to a grossly distorted result . . . ' " 437 U.S. at 274. The mere threat that income not generated in the state will be taxed under a formula does not make the formula constitutionally defective. 437 U.S. at 278. Congress, not the Court, must enact national uniform rules for the division of income if it finds duplicative taxation a problem. 437 U.S. at 279.

Washington's B&O tax has been held to be fairly apportioned in previous cases. See *Department of Rev. v. Association of Wash. Stevedoring Cos.*, *supra*; *Standard Pressed Steel Co. v. Department of Rev.*, *supra*; *Chicago Bridge & Iron Co. v. Department of Rev.*, *supra*. Nonetheless, Taxpayers urge that, under *Armco*, the tax must now pass the "internal consistency" test articulated in *Container Corp. of Am. v. Franchise Tax Bd.*, *supra*, and cited in *Armco*. In applying that test, the court must hypothesize that every jurisdiction has adopted a tax identical to the tax in question; the result must be that no more than 100 percent of a single business's income is taxed by one state.

We agree with the Department that the "internal consistency" test articulated in *Container Corp.* and *Armco* does not apply to the determination whether the B&O tax is fairly apportioned. This is because Washington does not tax the income of a unitary business, but rather taxes only the privilege of manufacturing or selling within the state. Thus, respondent urges that Washington's tax is apportioned by "allocation"; that is, the tax is applied only to the value of products manufactured in Washington or to the gross proceeds of sales in Washington.

We do not read the *Armco* opinion to apply its "internal consistency" test to the question of whether a state gross receipts tax is fairly apportioned. We believe that it does not apply not only because of the appeal of the Department's argument, but because the *Armco* Court said nothing about the status of *Washington Stevedoring*. See 435 U.S. 734. If the "internal consistency"

requirement applied to the fair apportionment prong, *Washington Stevedoring* should be overruled for requiring a showing of actual harm to make out unfair apportionment. 435 U.S. at 746 & n.16. Further, speaking specifically of the tax challenged here, the Court said, "[w]hen a general business tax levies only on the value of services performed within the State, the tax is properly apportioned and multiple burdens logically cannot occur." 435 U.S. at 746-47.

## 2. Fairly related.

The *Armco* Court did not address the "fairly related to state services" prong. The controlling case is *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 69 L. Ed. 2d 884, 101 S. Ct. 2946 (1981). Certain Montana coal producers and their out-of-state customers argued that they should be permitted to show that the state's high coal severance tax was not fairly related to state services provided. The Court refused to view the fair relation test as a cost-benefit analysis of the taxes paid and services received. The test is basically a nexus test, with "the additional limitation that the *measure* of the tax must be reasonably related to the extent of the [taxpayer's] contact" with the state. 453 U.S. at 626. The Court declined to determine what a reasonable measure might be because (1) no usable legal test could adequately reflect the varied considerations that "inform a decision about an acceptable rate or level of state taxation", 453 U.S. at 628; and, hence, (2) this is a question more suited to the political process. The taxpayer's "substantial privilege of mining coal" provided sufficient nexus and the only benefit the state needed to show was that the taxpayer enjoyed the "privileges of living in an organized society, established and safeguarded by the devotion of taxes to public purposes." 453 U.S. at 628-29. See also *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434, 60 L. Ed. 2d 336, 99 S. Ct. 1813 (1979).

Manufacturing, or wholesaling, would also appear to be privileges comparable to mining so that the nexus requirement is

sufficiently met in the present case. Despite any warts Washington may suffer, the State can show that ours is "an organized society." While local manufacturer-sellers enjoy "two activities for the price of one", interstate businesses cannot, under this prong, apply a cost-benefit analysis to show how they have been short-changed.

We believe the Washington B&O tax continues to meet commerce clause standards. We do not believe *Armco* requires the result urged by appellants and can be reconciled with compelling precedent not overruled in *Armco* and with scholarly commentary. We also believe the controlling facts in *Armco* differ significantly from those before us. The trial court is affirmed.

We concur:

---

---

---

---

---

---

---

---

---

---

IN THE SUPREME COURT  
OF THE STATE OF WASHINGTON

TYLER PIPE INDUSTRIES, INC.,  
a Delaware Corporation,

*Appellant,*

v.

STATE OF WASHINGTON,  
DEPARTMENT OF REVENUE,

*Respondent.*

MANDATE  
No. 51110-1  
Thurston County  
No. 812007314

The State of Washington to: The Superior Court of the  
State of Washington in and for Thurston County

This is to certify that the opinion of the Supreme Court of the State of Washington filed on March 6, 1986, became the decision terminating review of this court in the above entitled case on March 26, 1986. This cause is mandated to the superior court from which the appeal was taken for further proceedings in accordance with the attached true copy of the opinion.

Pursuant to Rule of Appellate Procedure 14.3, costs are taxed as follows:

\$380.22 in favor of respondent State of Washington,  
Department of Revenue and against appellant Tyler Pipe Industries, Inc.

E-2

IN TESTIMONY WHEREOF, I have hereunto set my hand  
and affixed the seal of said Court at Olympia, this 27th day of  
March, A.D. 1986

---

Reginald N. Shriver  
*Clerk of the Supreme Court,*  
*State of Washington*

cc:

Cartano, Botzer, Larson & Birkholz

Mr. Thomas McKinnon

Mr. Thomas Sterken

Hon. Ken Eikenberry

Attorney General

Mr. James Tuttle, Asst.

Reporter of Decisions

F-1

**IN THE SUPREME COURT  
OF THE STATE OF WASHINGTON**

TYLER PIPE INDUSTRIES, INC.,  
a Delaware Corporation,

*Appellant,*

v.

STATE OF WASHINGTON  
DEPARTMENT OF REVENUE,

*Respondent.*

No. 51110-1  
Filed April 15, 1986

**NOTICE OF APPEAL**

Notice is hereby given that Tyler Pipe Industries, Inc., appel-  
lant, hereby appeals to the Supreme Court of the United States  
from the opinion and judgment entered in this action on the 6th  
day of March, 1986. This appeal is prosecuted pursuant to 28  
U.S.C. Section 1257(2).

**CARTANO, BOTZER, LARSON &  
BIRKHOLZ**

By: \_\_\_\_\_

Thomas A. Sterken

25th Floor

One Union Square

Seattle, WA 98101

**CERTIFICATE OF SERVICE**

It is hereby certified that service of the foregoing Notice of Appeal was made this 14th day of April, 1986, upon all parties required to be served by depositing a copy thereof in the United States Mail, first class postage prepaid, addressed to:

Mr. Kenneth O. Eikenberry,  
Attorney General  
Mr. James R. Tuttle,  
Assistant Attorney General  
Department of Revenue  
AX-02  
415 General Administration Building  
Olympia, WA 98504

---

Mr. Thomas A. Sterken  
Cartano, Botzer, Larson & Birkholz  
25th Floor  
One Union Square  
Seattle, WA 98101

**APPENDIX G**

Constitution of the United States:

**Article I, Section 8, Clause 3**

The Congress shall have Power \*\*\* To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes;

**Amendment XIV**

Section 1. All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

United States Code, Title 15:

**§ 381. Imposition of net income tax**

(a) **Minimum standards.** No State, or political subdivision thereof, shall have power to impose, for any taxable year ending after the date of the enactment of this Act [enacted Sept. 14, 1959], a net income tax on the income derived within such State by any person from interstate commerce if the only business activities within such State by or on behalf of such person during such taxable year are either, or both, of the following:

- (1) the solicitation of orders by such person, or his representative, in such State for sales of tangible personal property, which orders are sent outside the State for approval or rejection, and, if approved, are filled by shipment or delivery from a point outside the State; and
- (2) the solicitation of orders by such person, or his representative, in such State in the name of or for the benefit of a prospective customer of such person, if orders by such customer to such person to enable such cus-

tomers to fill orders resulting from such solicitation are orders described in paragraph (1).

**(b) Domestic corporations; persons domiciled in or residents of a State.** The provisions of subsection (a) shall not apply to the imposition of a net income tax by any State, or political subdivision thereof, with respect to—

- (1) any corporation which is incorporated under the laws of such State; or
- (2) any individual who, under the laws of such State, is domiciled in, or a resident of, such State.

**(c) Sales or solicitation of orders for sales by independent contractors.** For purposes of subsection (a), a person shall not be considered to have engaged in business activities within a State during any taxable year merely by reason of sales in such State, or the solicitation of orders for sales in such State, of tangible personal property on behalf of such person by one or more independent contractors, or by reason of the maintenance of an office in such State by one or more independent contractors whose activities on behalf of such person in such State consist solely of making sales, or soliciting orders for sales, of tangible personal property.

**(d) Definitions.** For purposes of this section—

- (1) the term “independent contractor” means a commission agent, broker, or other independent contractor who is engaged in selling, or soliciting orders for the sale of, tangible personal property for more than one principal and who holds himself out as such in the regular course of his business activities; and
- (2) the term “representative” does not include an independent contractor.

Revised Code of Washington:

#### **82.04.220 Business and occupation tax imposed**

There is levied and shall be collected from every person a tax for the act or privilege of engaging in business activities.

Such tax shall be measured by the application of rates against value of products, gross proceeds of sales, or gross income of the business, as the case may be.

#### **82.04.230 Tax upon extractors**

Upon every person engaging within this state in business as an extractor; as to such persons the amount of the tax with respect to such business shall be equal to the value of the products, including byproducts, extracted for sale or for commercial or industrial use, multiplied by the rate of forty-four one-hundredths of one percent;

The measure of the tax is the value of the products, including byproducts, so extracted, regardless of the place of sale or the fact that deliveries may be made to points outside the state.

#### **82.04.240 Tax on manufacturers**

Upon every person except persons taxable under subsections (2), (3), (4), (5), (6), (8), (9), or (10) of RCW 82.04.260 engaging within this state in business as a manufacturer; as to such persons the amount of the tax with respect to such business shall be equal to the value of the products, including byproducts, manufactured, multiplied by the rate of forty-four one-hundredths of one percent.

The measure of the tax is the value of the products, including byproducts, so manufactured regardless of the place of sale or the fact that deliveries may be made to points outside the state.

#### **82.04.250 Tax on retailers**

Upon every person except persons taxable under subsection (9) of RCW 82.04.260 engaging within this state in the business of making sales at retail, as to such persons, the amount of tax with respect to such business shall be equal to the gross proceeds of sales of the business, multiplied by the rate of forty-four one-hundredths of one percent.

**82.04.270 Tax on wholesalers, distributors**

(1) Upon every person except persons taxable under subsections (1) or (9) of RCW 82.04.260 engaging within this state in the business of making sales at wholesale; as to such persons the amount of tax with respect to such business shall be equal to the gross proceeds of sales of such business multiplied by the rate of forty-four one-hundredths of one percent.

(2) The tax imposed by this section is levied and shall be collected from every person engaged in the business of distributing in this state articles of tangible personal property, owned by them from their own warehouse or other central location in this state to two or more of their own retail stores or outlets, where no change of title or ownership occurs, the intent hereof being to impose a tax equal to the wholesaler's tax upon persons performing functions essentially comparable to those of a wholesaler, but not actually making sales: *Provided*, That the tax designated in this section may not be assessed twice to the same person for the same article. The amount of the tax as to such persons shall be computed by multiplying forty-four one-hundredths of one percent of the value of the article so distributed as of the time of such distribution: *Provided*, That persons engaged in the activities described in this subsection shall not be liable for the tax imposed if by proper invoice it can be shown that they have purchased such property from a wholesaler who has paid a business and occupation tax to the state upon the same articles. This proviso shall not apply to purchases from manufacturers as defined in RCW 82.04.110. The department of revenue shall prescribe uniform and equitable rules for the purpose of ascertaining such value, which value shall correspond as nearly as possible to the gross proceeds from sales at wholesale in this state of similar articles of like quality and character, and in similar quantities by other taxpayers: *Provided further*, That delivery trucks or vans will not under the purposes of this section be considered to be retail stores or outlets.

**82.04.290 Tax on other business or service activities**

Upon every person engaging within this state in any business activity other than or in addition to those

enumerated in RCW 82.04.230, 82.04.240, 82.04.250, 82.04.255, 82.04.260, 82.04.270, 82.04.275 and 82.04.280; as to such persons the amount of tax on account of such activities shall be equal to the gross income of the business multiplied by the rate of one percent. This section includes, among others, and without limiting the scope hereof (whether or not title to materials used in the performance of such business passes to another by accession, confusion or other than by outright sale), persons engaged in the business of rendering any type of service which does not constitute a "sale at retail" or a "sale at wholesale." The value of advertising, demonstration, and promotional supplies and materials furnished to an agent by his principal or supplier to be used for informational, educational and promotional purposes shall not be considered a part of the agent's remuneration or commission and shall not be subject to taxation under this section.

**82.04.440 Persons taxable on multiple activities**

Every person engaged in activities which are within the purview of the provisions of two or more of sections RCW 82.04.230 to 82.04.290, inclusive, shall be taxable under each paragraph applicable to the activities engaged in: *Provided*, That persons taxable under RCW 82.04.250 or 82.04.270 shall not be taxable under RCW 82.04.230, 82.04.240 or subsection (2), (3), (4), (5), (6), or (8) of RCW 82.04.260 with respect to extracting or manufacturing of the products so sold, and that persons taxable under RCW 82.04.240 or RCW 82.04.260 subsection (4) shall not be taxable under RCW 82.04.230 with respect to extracting the ingredients of the products so manufactured.

**82.04.500 Tax part of operating overhead**

It is not the intention of this chapter that the taxes herein levied upon persons engaging in business be construed as taxes upon the purchasers or customers, but that such taxes shall be levied upon, and collectible from, the person engaging in the business activities herein designated and that such taxes shall constitute a part of the operating overhead of such persons.